UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, Linda Breathitt,
And Nora Mead Brownell.

El Paso Natural Gas Co.	Docket No. RP00-336-002
Aera Energy, LLC, et al., Complainants v. El Paso Natural Gas Co., Respondent	Docket No. RP01-484-000
Texas, New Mexico and Arizona Shippers, Complainants v. El Paso Natural Gas Co., Respondent	Docket No. RP01-486-000
KN Marketing, L.P., Complainant v. El Paso Natural Gas Co., Respondent	Docket No. RP00-139-000

ORDER ON CAPACITY ALLOCATION
AND COMPLAINTS

(Issued May 31, 2002)

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ORDER ON CAPACITY ALLOCATION
AND COMPLAINTS

This order resolves issues in four non-consolidated proceedings, all of which concern capacity allocation on El Paso Natural Gas Company's (El Paso) system. As discussed below, the Commission finds pursuant to section 5 of the Natural Gas Act (NGA), that the application of El Paso's current capacity allocation methodology is unjust and unreasonable and adversely affects the public interest because parties with firm transportation contracts are not receiving the firm service for which they are paying. Therefore, this order directs El Paso to modify its capacity allocation methodology to assure greater predictability for firm shippers.

This order directs that full requirements (FR) contract shippers on El Paso will be converted to service under contract demand (CD) contracts, effective November 1, 2002. The order provides the parties with a short period of time to reach an agreement as to the FR customers' entitlements under their new CD contracts. If the parties do not agree as to the appropriate CD entitlements, the Commission will determine the appropriate CD levels. Small shippers will be permitted to retain full requirements service under El Paso's Rate Schedule FT-2 as long as their requirements remain less than 10,000 Dth/d. Additionally, as explained below, the Commission will require an assignment of primary receipt rights to shippers, and allow El Paso to increase the number of pooling points on its system from 6 to 8. The Commission also directs El Paso to revise its tariff to establish flexible delivery/receipt points at the California border. With respect to allocable capacity, the Commission will conditionally require El Paso to accept turnbacks of existing CD entitlements and expects El Paso to follow through in its offer to seek authorization and place into service its Line 2000 PowerUp Project. This order also directs El Paso to pay demand charge credits if it is unable to schedule firm service for reasons other than force majeure.

Together, these capacity allocation measures appropriately balance the interests of all the parties to this proceeding and are in the public interest because they will resolve the current uncertainty on El Paso's system and assure that firm shippers receive the firm service to which they are entitled, consistent with Part 284 of the Commission's regulations[1] and section 5 of the Natural Gas Act (NGA). In addition, the capacity allocations will establish the proper market incentives for expansion of the infrastructure.

I. Background

[1] 18 C.F.R. Part 284 (2001).

El Paso operates a gas pipeline system that can deliver gas from three production basins, i.e., San Juan, Permian, and Anadarko, to various delivery points on its system. In recent years, gas supplies from the San Juan Basin have been less expensive than gas from the Permian and Anadarko Basins, making the San Juan Basin the preferred production area of El Paso's customers.[2] While the Commission has held that where it is operationally feasible, a pipeline should assign customers specific capacity rights at receipt and delivery points,[3] El Paso does not do so. Instead, in most instances, El Paso's contracts for firm transportation service provide for system-wide access to receipt and delivery points, and customers have no specified rights to pipeline capacity. If shippers' nominations exceed the physical capacity of a specific receipt point, El Paso's tariff provides for pro-rata allocation based on the nominated amount.

The issue of system-wide delivery points was addressed by the Commission in Amoco Energy Trading Co. v. El Paso Natural Gas Co. (Topock).[4] In Topock, the Commission found that El Paso's pro rata allocation of capacity at Topock and other delivery points was unjust and unreasonable because firm shippers were not receiving reliable firm service. The Commission ordered El Paso to assign specific delivery point rights. The Commission further ordered El Paso to file a proposal to allocate receipt point capacity.

El Paso has historically served its firm customers under two types of contracts: CD and FR contracts. CD contracts provide specific delivery rights up to a specified quantity limitations at delivery points designated in the contract. FR contracts provide that El Paso must deliver and the customer must take from El Paso, the customer's full natural gas requirements each day. In 1990, El Paso implemented contract conversions from bundled sales service to transportation service through a Global Settlement with its customers.[5] The Global Settlement specifically provided for the continuation of FR

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[2]For example, the "Monthly Index" in the "Monthly Contract Index" reported for El Paso in the January 2002 Gas Daily Price Guide is \$2.56/MMBTU for the Permian Basin and \$2.48/MMBtu for the San Juan Basin. The bid week low-high is reported as \$2.42-75 in the Permian Basin and \$2.30-63 in the San Juan Basin.

[3]Transcontinental Gas Pipe Line Co., 76 FERC ¶ 61,021 at 61,063 (1996).

[4]93 FERC ¶ 61,060 (2000), order on clarification, 93 FERC ¶ 61,222 (2000), order on reh'g, 94 FERC ¶ 61,225 (2001).

[5]54 FERC ¶ 61,316, reh'g, 56 FERC ¶ 62,290 (1991).

service.[6] The CD contracts are held mainly by customers that serve the California markets. The FR contracts are held mainly by customers east of California (EOC). Full requirements customers are not limited to a specific contract demand quantity. Like the CD contracts, FR contracts have system-wide primary receipt point rights. This means that shippers are free to nominate from any basin or pool to satisfy their needs. Under the General Terms and Conditions of El Paso's tariff,[7] if El Paso has insufficient capacity to serve all transportation requests at a nominated receipt pool, the firm shippers are subject to pro-rata cuts based upon available capacity.

On March 15, 1996, El Paso filed another settlement (1996 Settlement) that set the current rates, and terms and conditions of service that apply on its system for a ten-year period, i.e., until January 1, 2006. The 1996 Settlement also imposes a ten-year moratorium, under which El Paso cannot file for a general rate change and the parties may not file a section 5 complaint challenging the Settlement rates. The Commission approved the 1996 Settlement.[8] At the time the 1996 Settlement was filed, there was substantial excess capacity on El Paso's system, as the California LDC customers turned back capacity rights in accordance with their contracts. This capacity turn-back threatened to increase the rates of the remaining El Paso customers.[9] The 1996 Settlement resolved the capacity turnback problem through an agreed-upon sharing of the risk of unsubscribed or undersubscribed capacity.

Under the terms of the 1996 Settlement, the CD customers pay a reservation charge pursuant to Rate Schedule FT-1 based on their contract entitlements. The Rate Schedule FT-1 FR customers pay reservation fees based on their billing determinants as established in the 1996 Settlement.[10] The reservation fees have remained unchanged while many of the FR shippers' demands have grown; the result is that the FR shippers

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[6] Section 3.6 of the Settlement provides in part: It is further stipulated and agreed that El Paso's east-of-California customers may convert their existing firm sales entitlements to either firm full requirements or firm contract demand service...or a combination of both.

[7] GT&C, Section 4.2.

[8] 79 FERC ¶ 61,028, reh'g denied, 80 FERC ¶ 61,084 (1997).

[9] See 89 FERC ¶ 61,164 at 61,489 (1999).

[10] Additionally, under Rate Schedule FT-2, El Paso serves various small EOC customers on a volumetric rate basis. Unless otherwise noted, reference to FR shippers in this order will refer to Rate Schedule FT-1 FR shippers.

pay only a small usage charge for their incremental takes above the Settlement billing determinants.

Circumstances on El Paso's system have changed dramatically since 1996, when excess capacity and capacity turn-back were problems on the system. The turned-back capacity has been resold, and the FR shippers' load has grown. There is now insufficient capacity to meet the demands of all firm shippers. As explained above, gas from the San Juan Basin is preferred by El Paso's shippers because it is less expensive than gas from the Permian or Anadarko Basins. The preference for the San Juan Basin gas, together with the growth in demand from the FR shippers and the lack of incentives to expand the infrastructure have caused all firm shippers to experience frequent pro-rata nomination reductions. Many FR shippers have, nevertheless, received service in quantities that exceed their 1996 Settlement billing determinant levels. This has resulted in tension between the FR and CD customers which underlies each of the proceedings addressed in this order.

II. Procedural History

The four proceedings addressed in this order grow out of the increasing unreliability of firm service on El Paso. The first of the three complaints addressed in this order was filed by KN Marketing on December 16, 1999, alleging that El Paso's allocation of firm mainline capacity on the east end of its system, i.e. the San Juan Basin to Texas, is unjust and unreasonable because El Paso sells firm capacity in excess of the available capacity. In its order in Amoco Energy Trading Company v. El Paso Natural Gas Co. (Topock),[11] the Commission held the issues raised by the KN complaint in abeyance pending examination of system-wide capacity allocation issues in El Paso's Order No. 637 proceeding. The Commission directed El Paso to file a systemwide capacity allocation proposal in its Order No. 637 proceeding, and provided for parties to submit comments on El Paso's proposal. On March 28, 2001, El Paso filed its system-wide capacity allocation proposal in the Order No. 637 proceeding (i.e., Docket No. RP00-336-002). El Paso proposes to allocate capacity to the FR shippers based on their 1996 Settlement billing determinants. Commenters on El Paso's proposal recommended alternative methods for allocating capacity, including a proposal by Salt River Project to use FR shippers' historical non-coincidental peak demands.

After El Paso made its capacity allocation filing, two additional complaints were filed, one by a group of El Paso's CD shippers and one by a group of El Paso's FR

[11] 93 FERC ¶ 61,060 (2000), order on clarification, 93 FERC ¶ 61,222 (2000), order on reh'g, 94 FERC ¶ 61,225 (2001).

shippers, concerning capacity allocation issues. On July 13, 2001, a group of El Paso's California CD customers filed a complaint in Joint Complainants[12] v. El Paso, Docket No. RP01-484-000, alleging that El Paso had oversold its firm capacity and that this, combined with the growth of the demand of the FR customers, has resulted in unjust and unreasonable services on the El Paso system. On July 17, 2001, a group of El Paso's FR customers filed a complaint in Texas, New Mexico, and Arizona Shippers[13] v. El Paso, Docket No. RP01-486-000, alleging that El Paso violated the NGA by failing to maintain its facilities in a manner that will allow it to provide firm service up to certificated levels.

Details of El Paso's proposal and the alternative capacity allocation proposals before the Commission are set forth in Appendix A. The timely motions to intervene in the four proceedings are granted pursuant to Rule 214 of the Commission's Rules of Practice and Procedure. 18 C.F.R. § 385.214 (2001).

III. Discussion

All of the captioned proceedings involve the issue of whether El Paso's application of the capacity allocation mechanism in section 4.2 of its General Terms and Conditions (GT&C) is just and reasonable. Underlying issues are the extent to which unrestricted growth under the FR contracts has produced unjust and unreasonable results vis-a-vis El Paso's other firm services,[14] whether FR contracts should be converted to CD contracts

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[12]Joint Complainants are Aera Energy LLC (Aera), Amoco Production Company (Amoco), BP Energy Company (BP), Burlington Resources Oil & Gas Company LP (Burlington), Conoco, Inc (Conoco), Coral Energy Resources LP (Coral Energy), ONEOK Energy Marketing & Trading Company, L.P. (Oneok), Pacific Gas and Electric Company (PG&E), Panda Gila River L.P. (Panda Gila), the Public Utilities Commission of the State of California (CPUC), Southern California Edison Company (SoCalEdison), and Texaco Natural Gas Inc. (Texaco).

[13]These shippers are Apache Nitrogen Products, Inc. (Apache), Arizona Electric Power Cooperative, Inc. (AEP), Arizona Gas Division of Citizens Communication Company (Citizens Communication), BHP Cooper, Inc. (BHP), El Paso Electric Company (El Paso Electric), El Paso Municipal Customer Group (EPMCG), Phelps Dodge Corporation (Phelps Dodge), New Mexico PSC, Salt River Project (Salt River), and Southern Union Gas Company (Southern Union).

[14]El Paso's design day delivery capacity is approximately 5,400,000 Dth/d. CD entitlements total 4,316,000 Dth/d. Current CD entitlements and FR demands exceed the capacity of the El Paso system. At the time of the 1996 Settlement, FR billing

(continued...)

and, if so, at what CD entitlement levels. In addition, the parties have raised issues concerning whether El Paso is obligated to expand its system to meet the needs of its firm shippers and whether El Paso should be required to provide demand charge credits to firm shippers that pay demand charges for volumes El Paso is unable to transport. The Commission will address these issues below, and then will apply its conclusions on each issue to the individual proceedings.

For the reasons discussed below, the Commission concludes that as a result of a lack of specified receipt point entitlements in El Paso's tariff, the frequent pro rata allocation of firm capacity on El Paso's system,[15] and the lack of proper price signals for the expansion of the infrastructure, El Paso's current capacity allocations are no longer just and reasonable nor in the public interest. Therefore, the Commission must act under section 5 of the NGA to establish just and reasonable firm service entitlements that are in the public interest. The Commission finds that the rapid and unrestricted growth in demand under the FR contracts has contributed to the current allocation problems on the system, and that continued unlimited growth in demand under these FR contracts is not just and reasonable and is not in the public interest. Therefore, the Commission finds that the Rate Schedule FT-1 FR contracts should be converted to CD contracts, effective November 1, 2002. Rate Schedule FT-2 service should be capped at a demand level of 10,000 Dth/d. All firm shippers must be assigned specific receipt and delivery point rights under their contracts.[16] Conversion of FR contracts to CD contracts, coupled with the assignment of specific point rights, will restore certainty to firm service, assure that

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[14](...continued)
determinants were 788,039 Dth/d. The FR coincident peak demand for December 12, 2001 was 1,122,000 Dth/d. The FR non-coincident peak demand for 1995 was 1,092,181 Dth/d while in 2001, the total FR non-coincident peak demand was 2,167,107 Dth/d. In addition, while demands on El Paso's system historically peaked during the winter heating season months, El Paso's customers have increased their nominations during historical non-peak periods, primarily to serve electric generation demands.

[15]The pro rata allocations of capacity made by El Paso based on the customers' nominations result in cuts to the amounts nominated by the customers and the failure to schedule service for the full nominated volumes. In the case of the CD customers, demand charges have already been paid for this capacity, and the customers therefore do not receive the service they are paying for.

[16]As noted above, in Topock the Commission required El Paso to establish specific delivery point rights under CD service. 93 FERC ¶ 61,222, reh'g, 94 FERC ¶ 61,225 (2001).

firm shippers receive the service they are paying for, and establish the proper price signals for expansion of capacity.

The appropriate level of CD entitlements therefore must be determined for each FR shipper. The Commission discussed several methods of establishing CD entitlements for the FR shippers at its March 13, 2002 meeting, and directed that a public conference be held to discuss the various methodologies, including the use of system peak day demands. At the public conference held on April 16, 2002 and in the written comments[17] filed on the proposal to use the system peak to establish CD levels, the FR shippers expressed concern that they be provided sufficient capacity to meet their summer and winter season demands. As explained more fully below, the Commission will afford the parties an opportunity to establish entitlements under the new CD contracts to reflect seasonal usage. After determining the appropriate CD entitlement for each customer, El Paso shall initiate a capacity rationalization process to make additional capacity available to the converting customers by providing an opportunity for shippers to turnback unwanted capacity and for converting shippers to request and purchase additional capacity. In this process, all shippers will have an opportunity to establish specific receipt point rights. If the parties are unable to reach an agreement on appropriate CD entitlements for the FR shippers, the Commission will determine the appropriate CD entitlement for the FR shippers.

A. El Paso's Application of Capacity Allocation Procedures Is No Longer Just and Reasonable Nor in the Public Interest

As is explained in more detail below, the Commission finds that El Paso's capacity allocation methodology, as it operates currently, is no longer just and reasonable because it results in regular reductions in firm service. As a consequence, CD shippers have sustained substantial harm.

There is no disagreement among the parties that firm shippers on El Paso have been subject to, on a regular and continuing basis, pro rata allocations of their daily nominations of firm capacity. At the April 16, 2002 public conference, El Paso admitted that it no longer had sufficient capacity to meet the demands of its customers.[18] The CD customers assert that because of the service reductions that result from these allocations, they cannot use the firm capacity that they have under contract and pay for, and that they

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[17]The comments of the parties filed in connection with the April 16, 2002 public conference are summarized in Appendix B.

[18]Transcript of Public Conference, April 16, 2002 (Tr.) at 13 and 18.

and the downstream markets they serve are financially harmed on a routine basis. In the complaint proceeding in Docket No. RP01-484-000, Joint Complainants submitted affidavits, as discussed in Appendix C, asserting that nomination scheduling cuts on El Paso have cost them millions of dollars in stranded demand costs.[19] CD shippers filed updated affidavits after the April 16 Public Conference. BP Energy, for example, in an affidavit by Russell Williamson, states that its cycle four cuts[20] were 40,063,202 MMBtu from January 1999 through December 31, 2001, resulting in stranded demand charges of $10,132,998.

The CD shippers point out that if APS/Pinnacle is permitted to increase deliveries to the new Redhawk plant in the Fall of 2002, APS/Pinnacle demands would increase by over 600 percent over its billing determinants and cause further service reductions to CD shippers. Further, the EOC growth in demand is projected to continue. The Arizona Corporation Commission noted that new electric generation is under construction in Arizona to meet the extraordinary growth in Arizona's need for natural gas; nearly 4,000 additional megawatts in electric generation capacity is scheduled to be completed within a year, and another 4,000 megawatts of generation capacity is approved or under construction for completion by the end of 2003.[21] Most, if not all, of this new generation capacity is projected to be fueled with natural gas.

The TNMA FR shippers agree that there are serious allocation problems on El Paso, and state that the system is in "full crisis"[22] with daily reductions in firm service as standard operating procedure. El Paso does not dispute the assertion that significant pro rata allocations in firm service nominations are taking place on a routine basis. El Paso states that in making these pro rata allocations, it has acted consistently with its tariff, the Settlements and customers' contracts. El Paso agrees with Joint Complainants that if it is

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[19]Stranded demand costs refer to dollars spent by the CD customers in demand charges for capacity that El Paso does not make available to them due to pro rata allocations.

[20]Cycle four is the last nomination cycle for the gas day. Cuts to cycle four nominations, therefore, are volumes that the shipper will not receive, for there are no subsequent opportunities that gas day to nominate at a different receipt point or from a different pipeline.

[21]Tr. at 48.

[22]Protest and Comments of Texas, New Mexico and Arizona Shippers, Docket No. RP01-484-000 filed August 2, 2001 at p. 9.

required in the future to serve unlimited demands of its FR customers, its current inability to provide firm service to those shippers paying for that firm service will be exacerbated.

APS/Pinnacle assert that a solution that caps FR service is discriminatory in its treatment of one class of customers and is therefore unreasonable. The Commission disagrees that the solution is unreasonable. The Commission is convinced that further increases under full requirements contracts will further degrade the quality of CD service and cause corresponding, equivalent decreases in service to CD shippers. Increases in demand of the magnitude required for the APS/Pinnacle Redhawk Plant will significantly degrade CD service and result in further harm. The Commission will not allow service to one group of firm customers to cause sustained financial harm to another group of firm customers.

The Commission finds, based on the representations of all of the parties in this proceeding, that El Paso does not have sufficient firm capacity to meet growing demand for firm service on its system, and firm service has been curtailed through pro rata allocations of service nominations on a routine basis.[23] Capacity allocation procedures that result in regular cuts in firm service are not just and reasonable. Pro rata allocation is an appropriate way to deal with emergency circumstances, but it cannot be a regular part of the daily scheduling process. For El Paso's capacity allocation methodology to be just and reasonable, a firm shipper must be able to reliably schedule its firm contractual entitlements without service reductions except for force majeure.[24]

As a consequence of demand growth and pro rata allocations on El Paso, the firm CD shippers have been unable to use the full amounts of their firm contract entitlements. Effectively, these customers pay demand charges for capacity they are unable to use. Section 284.7 of the Commission's regulations provides that firm service is service that is not subject to a prior claim by another customer.[25] It is inconsistent with this regulation for firm shippers to be charged for firm service and have service reduced through pro rata allocations on a non-emergency basis so that the pipeline can provide service to another shipper. A shipper contracting for firm service, as compared to interruptible, pays the pipeline a charge to reserve capacity on the pipeline in addition to the volumetric charge for actually transporting the gas. If the reservation portion of the firm transportation rate

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[23]See El Paso Data Response, filed August 23, 2001. Response No. 4 shows that El Paso made in excess of 10,000 pro rata allocations of service nominations between August 2000 and July 2001.

[24]Topock, 93 FERC ¶ 61,060 at 61,161.

[25]18 C.F.R. § 284.7 (2001).

does not in fact reserve capacity on the pipeline, that charge must be unjust and unreasonable because the shipper is paying for a service that it cannot receive.

In their post-technical conference comments in Docket No. RP00-336-002, APS/Pinnacle states that it is improper to apply the principles governing firm service on other pipelines to the El Paso system. APS/Pinnacle states that the mere existence of the pro rata allocation methodology for allocating available capacity among firm shippers on the El Paso system means that firm capacity is not analogous to firm capacity on other pipelines. Contrary to the suggestion of APS/Pinnacle, the Commission's regulations that define firm service apply to firm service on all pipelines. Firm service has the same attributes and must meet the same requirements on all pipelines. The Commission has not approved a different type of firm service on El Paso that is less firm or less reliable than firm service on other pipelines.

Moreover, service nomination strategies exacerbate the need for nomination allocations. El Paso's tariff provides for system-wide primary point access to receipt points, and pro rata allocations if nominations exceed capacity. CD customers cannot nominate quantities above their CD levels, but the FR shippers can and must nominate their full gas requirements, and thus do not have a specific volumetric limit on the quantities they can nominate. The FR shippers' nominations are limited only by the capacity of their delivery points. Non-specific primary receipt point rights and the pro rata allocation methodology were not issues at the time of the 1996 Settlement because there was excess capacity on El Paso at that time.

In the Topock proceeding, the Commission determined that El Paso's practice of prorationing primary firm capacity at the Topock delivery point and other delivery points was unjust and unreasonable because firm shippers were not receiving reliable firm service. The same reasoning is applicable here, and the Commission concludes that unspecified primary point access to receipt points and El Paso's pro rata allocation methodology is unjust and unreasonable because firm shippers are not receiving firm service, contrary to section 284.7 of the Commission's regulations. The Commission will, therefore, again exercise its authority under section 5 of the NGA and direct El Paso to implement a plan to establish specific primary point rights at receipt points.

B. Full Requirements Contracts on El Paso Are No Longer Just and Reasonable Nor in the Public Interest

While, as discussed above, there is no disagreement among the parties that El Paso has insufficient capacity to meet the needs of its firm shippers and that cuts in firm service occur on its system, the parties disagree as to the cause of the problems and the appropriate solution. The CD customers and El Paso attribute the routine pro rata cuts, at least in part,[26] to growth in FR demand and assert that some limit must be placed on the growth in demand permitted under those contracts. El Paso maintains that it is not obligated to build pipeline capacity to meet growing demands. The FR shippers, on the other hand, argue that the CD shippers have not shown that the increase in FR demand has caused the pro rata allocations, that they are legally entitled to transport their daily requirements and that the solution to the problems on El Paso is to require El Paso to expand its system, not to limit the demand under FR contracts.

Using the customers' data posted on El Paso's website regarding demands on its system, Joint Complainants calculate that EOC FR load on El Paso has increased by approximately 50 percent from 1995 to January 2001. These data indicate that for the first years after the Settlement, demand under the FR contracts was relatively small and steady. Joint Complainants assert that in 1995, the peak FR demand was 1033 MMcf/d; in 1996 it was 1135 MMcf/d; and in 1998 it was 1127 MMcf/d. Subsequently, the demands have increased significantly. In 1999 FR demand was 1300 MMcf/d, in 2000 it was 1400 MMcf/d, and in January 2001 it was 1500 MMcf/d. The TNMA Shippers acknowledge that their demand has grown by approximately 9.5 percent per year since the test period.[27] Again, there is no disagreement among the parties regarding the underlying facts, and that the volumes demanded under the FR contracts have grown significantly since the execution of the 1996 Settlement, approximately 50 to 70 percent. El Paso's August 16, 2001 data response projects that demand under the FR contracts will grow to over 2 Bcf in 2002.[28] In fact, FR shippers have now projected that their need in aggregate will total 3 Bcf over the next few years.

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[26]The CD customers also allege that the problem has been caused in part by El Paso overselling its system.

[27]They state that in the 1994-1995 test period, the aggregate FR non-coincident peaks were 969,961 Dth. They state that multiplying that number by 9.5 percent over six years equals 1,672,011 Dth, which is approximately equal to the 2000 aggregate FR of 1,664,294 Dth. This calculates to a growth in demand of 72 percent for the period 1994-1995 to 2000.

[28]The data response includes studies containing FR shippers' projected demand through December 2006. Study 4A shows that FR shippers project peak demands in excess of 2.8 Bcf. Joint Complainants state that additional planned electric generation projects in the Southwest, if constructed, will require an additional 2200-2900 Mmcf/d of capacity by 2004. Joint Complainants, pp. 19-20 and Exhibit E.

The FR shippers[29] argue, however, that the Joint Complainants have failed to show that the increase in FR demand is the cause of the reduction in service due to the pro rata allocations to firm service. APS/Pinnacle states that the complaint is void of any quantitative analysis of new capacity commitments entered into by El Paso since 1995 that could contribute to the problem.

The Commission does not suggest that there is a single cause of the capacity crisis on El Paso. As APS/Pinnacle suggests, El Paso has continued to remarket firm service capacity as contracts expire irrespective of current capacity availability on its system, and the impacts its actions may have on all other shippers.[30] Nonetheless, while the growth in FR demand may not be the only cause of the service degradation problem, it is the most significant part of the problem and any solution must tie future growth in FR customers' demands to appropriate allocations of costs related to those demands as well as to capacity expansions, so that this growth does not negatively impact service rights of other firm shippers. Plans for new gas-fired power plants indicate that future FR growth would be substantial, further exacerbating the situation. For example, APS's proposed Redhawk generation facility, projected to be in service in Fall 2002, seeks to obtain 410,000 Mcf/d under APS's FR contract, increasing APS's FR usage by over 600% from its billing determinant of 66,000 Mcf/d.[31] FR growth would greatly increase if this capacity were supplied under the FR contracts and the increased demand would cause additional cuts in firm CD service. In addition, these increases take place without any added revenue responsibility and provide no incentive for El Paso to build additional facilities.

The Commission finds that where capacity is constrained on a pipeline, permitting increased demand growth under FR contracts will necessarily further degrade firm service and result in additional pro rata cuts to firm nominations. This is inconsistent with the concept of firm service and with the Commission's regulations.[32] Therefore, the Commission finds that it is necessary to convert the FR contracts to CD contracts to remedy the unjust and unreasonable impact unrestricted demand growth has on all firm

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[29] E.g., TNMA, APS/Pinnacle, and Southwest.

[30] In Docket No. RP97-287-057, El Paso Natural Gas Co., 99 FERC ¶ 61,140 (issued May 1, 2002), the Commission expressed concern that El Paso had not demonstrated that it has the capacity to serve PPL EnergyPlus, LLC (PPL) on a firm service basis and suspended the effectiveness of its firm service agreement with PPL for five months.

[31] Joint Complainants, p. 19.

[32] 18 C.F.R § 284.7.

shippers on the El Paso system. Continued unlimited growth of the FR contracts, without factoring rate and service consequences, is not in the public interest because it will continue to degrade firm service reliability.

In addition, the rates paid by the FR shippers do not ration capacity,[33] and provide unfair competitive advantages for new power plants that are served under existing FR contracts. Converting FR contracts to CD contracts will bring El Paso's operations more closely into compliance with the uniform business practices adopted by the North American Energy Standards Board (formerly GISB), Order Nos. 636[34] and 637,[35] and thus bring additional benefits to all of El Paso's customers. Further, because FR customers will have to bid for additional capacity, El Paso will have the economic incentive to build necessary capacity to serve growing demand.

The full requirements customers state that they must rely on the FR contracts because they are captive customers, yet FR contracts serve to keep them captive. The FR customers state that there has been significant growth in the population and economy of the region they serve. In a competitive market, there would be incentives for both El Paso and other pipelines to enter that market to supply and compete for the growth in business. However, the FR contracts remove that incentive since no new entrant to the market can compete with El Paso for customers that will have all their growth served

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[33]18 C.F.R. § 284.10(b)(1) (2001).

[34]Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation and Regulations of Natural Gas Pipelines After Partial Wellhead Decontrol, 57 Fed. Reg. 13,267 (April 16, 1992), FERC Stats. & Regs Preambles January 1991 - June 1996 ¶ 30,939 (April 8, 1992), order on reh'g, Order No. 636-A, 57 Fed. Reg. 36,128 (August 12, 1992), FERC Stats.& Regs. Preambles, January 1991 - June 1996 ¶ 30, 950 (August 3, 1992), order on reh'g, Order No. 636-B, 57 FED. REG. 57,911 (December 8, 1992), 61 FERC ¶ 61,272 (1992), notice of denial of rehearing (January 8, 1993), 62 FERC ¶ 61,007 (1993), aff'd in part and vacated and remanded in part, UDC v. FERC, 88 F.3d 1105 (D.C. Cir.1996), order on remand, Order No. 636-C, 78 FERC § 61,186 (1997), order on reh'g, Order No. 636-D, 83 FERC ¶ 61,210 (1998).

[35]Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services, FERC Stats. & Regs. Regulations Preambles (July 1996-December 2000) ¶ 31,091 (Feb. 9, 2000); order on rehearing, Order No. 637-A, FERC Stats. & Regs, Regulations Preambles (July 1996-December 2000) ¶ 31,099 (May 19, 2000), aff'd in part and rev'd and remanded in part, INGAA v. FERC, 285 F.3d 18 (D.C.Cir. 2002).

under their existing contracts. And, because FR customers are not subject to increased reservation charges with increases in demand, there is no economic incentive for El Paso to add needed capacity at Rate Schedule FT-1 commodity rates.[36] We find that the current FR contracts are a disincentive to pipeline-to-pipeline competition and provide no incentive for El Paso to provide for necessary expansion.[37] Once the FR contracts have been converted to CD contracts, FR customers will be able contractually to purchase transportation from pipelines other than El Paso. This will provide proper incentives and price signals for other pipelines to compete with El Paso and for El Paso to construct additional capacity to serve these needs.

The Commission's decision here is not premised on whether the level of growth in the FR demand was foreseeable at the time of the execution of the Settlement. The CD customers argue that full requirements contracts do not permit unlimited growth in demand, and do not permit growth that is unreasonably disproportionate to the expectation of the parties. SoCalGas cites caselaw decided under the Uniform Commercial Code (UCC) holding that a demand that is 60 percent in excess of an estimate is excessive,[38] and argues that therefore a several hundred fold increase in demand, such as sought by APS/Pinnacle, is an unacceptable modification of the FR contract. Similarly, in its comments filed at the April 16, 2002 public conference, Indicated Shippers argue that there are legal limits on the growth that can occur under full requirements contracts and that full requirements contracts should not be interpreted to permit unlimited growth.[39]

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[36]As discussed below, we conclude that the language of the Settlements does not place an unqualified obligation on El Paso to build additional facilities to serve FR growth, and conditions any such obligation on the economic feasibility of the construction. There appears to be no economic incentive for El Paso to construct facilities to serve customers that will pay only a commodity charge for use of the new facilities.

[37]It is true that El Paso has added the Line 2000 Project without any incremental surcharges. Line 2000 is the first phase of the conversion of the All American Pipeline to a natural gas pipeline, which will be integrated into the El Paso system in at least three separate stages.

[38]SoCalGas cites Shea-Kaiser-Lockheed-Healy v. Department of Water and Power (1977) 73 Cal.App.3d 679, 140 CalRptr. 884.

[39]Indicted Shippers cite, inter alia, Granite City Steel Co. v. FPC, 320 F.2d 711 (D.C.Cir. 1963).

The FR shippers,[40] on the other hand, argue that UCC case law is not applicable to these contracts. In any event, they argue, the type of growth that has occurred since the 1996 Settlement is consistent with the growth in the economy of the Southwest and was foreseeable at the time of the Settlement.[41] TNMA Shippers assert that the Commission has never placed quantitative limits on FR service and has repeatedly held that FR contracts entitle customers to take their full requirements daily.

The Commission recognizes that the courts have placed implied limitations on full requirements contracts. As the parties point out, these limitations are often related to foreseeability and the expectations of the parties. While the Commission is not suggesting that increases in demand under the FR contracts from new plants such as APS/Pinnacle's proposed Redhawk plant[42] were or should have been foreseeable at the time of the Settlement, even if they were, the Commission must consider the public interest in resolving capacity allocation issues where there is insufficient capacity on the pipeline to meet firm demand. The current routine reductions in firm service that will become greater as demand continues to grow without a concomitant increase in available capacity are not just and reasonable. Therefore, the Commission must provide a remedy that is in the public interest. It is the public interest, not whether these problems should have been foreseen at the time of the Settlement, that must guide the Commission's action.

Moreover, the Commission is establishing a procedure for the parties, in the first instance, to establish a reasonable limit on the amount of capacity that the FR customers can take in the future. The Commission believes that this procedure will allow El Paso and its customers to establish future CD entitlements for the current FR customers, taking into account the customers' needs. This approach is preferable to the Commission setting a limit on FR contracts based on its determination of what level of growth in those contracts was foreseeable and proportionate to the expectations of the parties.

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[40] E.g., APS/Pinnacle, TNMA Shippers, and Southwest Gas.

[41] TNMA Shippers cite statistics from the U.S. Census Bureau showing that between 1990 and 2000, the population of Arizona increased 40 percent, that of New Mexico by 20.1 percent, and that of Texas by 22.8 percent, compared to a 13 percent increase for the United States as a whole.

[42] See 95 FERC ¶ 61,461 (2001).

1. Conversion of the FR Contracts to CD Contracts Is Consistent with the Mobile-Sierra Doctrine

The FR shippers [43] argue that conversion of their contracts would involve material alterations of existing contracts, and that such changes cannot be made without meeting the higher public interest standard set forth in the Mobile-Sierra doctrine.[44] These parties argue that the Commission bears a heavy section 5 burden in abrogating existing contracts. APS/Pinnacle argues, citing Texaco, Inc. v. FERC,[45] that the Commission cannot rely on generic public interest findings in meeting this burden, but must make a particularized showing regarding the manner in which a particular contract harms the public interest and the extent to which abrogation or reformation mitigates the contract's deleterious effect.

The Joint Complainants, on the other hand, assert that Mobile-Sierra does not apply in these proceedings because some of the contracts for FR service provide for a future modification to the 1996 Settlement by the Commission and a renegotiation of the contracts to conform to any such modification.[46] The language cited by Joint Complainants, however, refers to any changes in the Settlement that might have been made by the Commission in its order approving the Settlement, not to changes to the Settlement after its approval. We find that the Mobile-Sierra doctrine applies in this case.

Under Mobile-Sierra, a pipeline cannot unilaterally change its contracts with its customers by making a section 4 filing. The Commission, however, retains its section 5 authority to modify contracts that it determines are not in the public interest. As the court

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[43] E.g., Joint Motion to Intervene and Answer of APS/Pinnacle in Docket No. RP01-484-000; Protest and Comments of TNMA Shippers in Docket RP01-484-000.

[44] FPC v. Sierra Pacific Power Co., 350 U.S. 348 (1956); United Gas Pipeline Co. v. Mobile Gas Service Corp., 350 U.S. 332 (1956).

[45] 148 F3d.1091, 1097 (D.C.Cir. 1998).

[46] The Joint Complainants cite language of the FR contracts that provides that if there is a change in the Settlement, the parties agree to negotiate in good faith to "conform this Agreement [the FR contract] to the Stipulation and Agreement as so changed or modified." Joint Complainants cite as an example, Article 9.10 of the FR contract between APS and El Paso.

stated in UDC v. FERC,[47] "[u]nder § 5, 'the Commission has plenary authority to limit or to proscribe contractual arrangements that contravene the relevant public interests.'" But, only in extraordinary circumstances, and only where the public interest so requires, will the Commission order contract modification.[48] For example, the Commission has ordered contract modification in connection with its restructuring of the natural gas[49] and electric industries.[50]

In Texaco, Inc. v. FERC, cited by APS/Pinnacle and the TNMA Shippers, shippers challenged the Commission's authority to require a pipeline to file tariff sheets imposing the Straight Fixed Variable (SFV) rate design on shippers whose contracts specified Modified Fixed Variable (MFV) rates, and argued that this was a contract modification prohibited by Mobile-Sierra. The court held that the Commission's modification of the existing contracts could be upheld only if the Commission showed that the public interest had required it to intervene. The court further stated that the public interest that permits FERC to modify a contract is different from and more exacting than the public interest that FERC seeks to serve when it promulgates its rules. The court stated that "more is required to justify regulatory intervention in a private contract than a simple reference to

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[47]88 F.3d 1105, 1131 (D.C. Cir. 1996), cert denied, 520 U.S. 1224 (1997) (quoting Permian Basin Area Rate Cases, 390 U.S. 784 (1968)). See also, e.g., Wisconsin Gas Co. v. FERC, 770 F.2d 1144 (D.C. Cir. 1985), 476 U.S. 1144 (1986).

[48]See, Nevada Power Co. v. Duke Energy Trading and Marketing, L.L.C., 99 FERC ¶ 61,047 at 61,190 (2002).

[49]Order No. 636, supra.

[50]Order No. 888 Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded costs Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities Order No. 888 , 61 Fed. Reg. 21,540, at 31,664-65 (1996), FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996 ¶ 31,036 (1996), order on reh'g, Order No. 888-A , 62 Fed. Reg. 12,274 (1997), FERC Statutes and Regulations, Regulations Preambles July 1996-December 2000 ¶ 31,048 (1997), order on reh'g, Order No. 888-B, 81 FERC ¶ 61,248 (1997), order on reh'g, Order No. 888-C, 82 FERC ¶ 61,046 (1998), aff'd in relevant part, remanded in part on other grounds sub nom. Transmission Access Policy Study Group, et al. v. FERC, 225 F. 3d 667 (D.C. Cir. 2000), aff'd, New York v. FERC, 122 S. Ct. 1012 (2002).

the policies served by a particular rule."[51] The court affirmed the Commission's orders, stating that the Commission did not rest its reformation of the contracts on only the broad public interest underlying its policy favoring SFV, but also explained how retention of MFV on the particular pipeline would threaten the coherence of the national policy and distort the local gas market. The court found that the Commission had satisfied its obligation to articulate supportable and reasonable explanations of how the public interest required modification of a private contract.

There are extraordinary circumstances on El Paso that require, in the public interest, modification of the FR contracts. The Commission's determination that the public interest requires modification of the FR contracts is not based merely on generalized statements of policy goals, but is based on a detailed analysis of how the FR contracts on El Paso harm the public interest and how the conversion of those contracts will further the public interest. The Commission has explained in detail how growth under the FR contracts has resulted in pro rata cuts that have eroded firm service on El Paso, and how this has resulted in firm shippers paying for service they do not receive. It is in the public interest to have reliable firm service on El Paso, and the Commission has explained how modification of the FR contracts on El Paso serves that goal. All customers will ultimately benefit from reliable firm service on El Paso and from the establishment of the proper market incentives for expansion of the infrastructure that will result from conversion of the FR contracts to CD contracts.

TNMA Shippers assert that the Commission has approved FR contracts for several decades, and to find now that FR service is contrary to the public interest would be an arbitrary reversal of its own finding. The fact that the Commission approved FR contracts in the past does not mean that the Commission cannot modify FR contracts as it has done here when those contracts operate in a manner that is contrary to the public interest. In fact, the Commission has an affirmative duty not to turn a blind eye to the degradation of firm service on El Paso's system. For example, when supply shortages arose in the natural gas industry in the 1970's, the Commission found itself "impelled to direct curtailment on the basis of end use rather than on the basis of contract simply because contracts do not necessarily serve the public interest requirement of efficient allocation of a wasting resource..."[52] Here, the Commission has clearly explained the reasons for conversion of the FR contracts to CD contracts.

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[51] 148 F.3d at 1097.

[52] Order No. 467, 49 F.P.C. 85, 86 (quoting Arkansas Louisiana Gas Co., 49 F.P.C. 53, 66 (1973), reh'g, 49 F.P.C. 583 (1973), petition for review dismissed sub nom., Pacific Gas & Electric Co. v. F.P.C., 506 F.2d 33 (D.C.Cir. 1974).

TNMA Shippers also argue that modification of the FR contracts is not in the public interest because the FR shippers are generally captive customers who have relied on and continue to rely on their contracts to provide utility service to human needs customers and to keep industrial plants running. However, it is the Commission's responsibility in the first instance, to decide whether the modification of the contracts is in the public interest taking all factors into account including whether maintaining the status quo "cast[s] upon other consumers an excessive burden, or [is] unduly discriminatory."[53] Moreover, as explained below, the limitation of future growth under the FR contracts is consistent with the Commission's duty to protect captive customers.

2. Conversion of the FR Contracts to CD Contracts Is Consistent With Section 7 of the NGA

The FR shippers argue that conversion of their contracts to CD contracts at the billing determinant level as proposed by El Paso in its allocation filing and by Joint Complainants in their complaint would constitute an unlawful abandonment of certificated full requirements service and substitute partial requirements service in its place.[54] These parties argue that an abandonment within the meaning of section 7(b) occurs whenever a natural gas company reduces a significant portion of a particular service dedicated to the interstate markets,[55] and when there is a reduction or alteration in overall service.[56] They argue that FR shippers are legally entitled to transport their daily requirements, and that full requirements service cannot be abandoned without a finding under section 7 of the NGA that abandonment is in the public interest.

These parties further argue that the Commission cannot make this public interest finding here because the FR shippers are, for the most part, captive customers that transport their daily full requirements to meet their utility obligations to their own

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[53]FPC v. Sierra Pacific Power Co., 350 U.S. 348, 355 (1955).

[54]See, e.g., Comments of East of California Shippers in Opposition to Indefinite and Unlawful Capacity Allocation Proposal, Docket No. RP00-336-000, filed May 17, 2001 at 21-22; Protest and Comments of TNMA Shippers in Docket No. RP01-484-000, filed August 2, 2001 at 10-15.

[55]The EOC Customers cite Reynolds Metals Co. v. FPC, 534 F.2d 379, 384 (D.C.Cir. 1976).

[56]The EOC Customers cite Tennessee Gas Pipeline Co. v. FERC, 972 F.2d 376, 384 (D.C.Cir. 1992).

customers. If their entitlements were reduced, these shippers argue,[57] it would be impossible for them to serve their own customers or maintain their business operations. TNMA Shippers allege that if entitlements were reduced, there would be rolling blackouts throughout Texas, New Mexico, and Arizona, and many businesses and communities would be harmed. Further, these parties argue, FR distributors and electric utilities serve human needs customers, and the curtailment of gas and electricity would have disastrous public health impacts on all sectors of the economy in the affected states. This result, they argue, is not consistent with the public convenience and necessity. Further, they argue, it contradicts the Commission's charge under section 7(b) of the NGA to protect the rights of existing shippers. Consistent with that obligation, TNMA Shippers argue, the Commission should find that El Paso has partially abandoned service to its firm customers and that El Paso must provide facilities to provide service to all firm customers.

The circumstances before us are very different from the circumstances in the cases cited by the FR customers. In this case, the Commission finds under section 5 of the NGA that continued growth in demand under the FR contracts imperils the provision of firm service on El Paso's system and thus is not just and reasonable in the current circumstances on El Paso's system. Therefore, the Commission is directing El Paso to convert these FR contracts to CD contracts and is providing the parties with an opportunity to establish a CD entitlement for these shippers that takes into account their current needs. As the Commission has explained, this conversion is necessary under section 5 of the NGA to protect all customers and the public interest and is consistent with the Mobile-Sierra doctrine.

The conversion of the FR contracts to CD contracts is also fully consistent with the requirements of section 7 of the NGA regarding abandonment of service and the Commission's obligation to protect captive customers. The protection afforded customers with regard to abandonment of their Part 284 service is intended to protect captive customers from the monopoly power of the pipeline and to permit captive customers to continue to receive the historical service upon which they have relied, as long as they are willing to pay the maximum rate for that service.[58] As the Commission explained in Order No. 637, this abandonment protection applies with regard to the captive customer's historical capacity. It is a limited right and is intended as a defense against the pipeline's

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[57] See, e.g., Protest and Comments of TNMA Shippers in Docket No. RP01-484-000.

[58] Order No. 636, aff'd in pertinent part, UDC v. FERC, 88 F.3d 1105 (D.C.Cir. 1996), cert. denied, 520 U.S. 1224 (1997); Order No. 637 at 31,335 - 340.

monopoly power, not as a mechanism to award an existing customer a preference in obtaining additional service.[59] Further, the protection against abandonment does not give a captive customer a right to discounted service in the future.[60] Continued growth in demand under the FR contracts and the addition of new facilities to be served under those contracts are not the within the scope of the abandonment protection.

The Commission is giving the parties an opportunity to establish CD entitlements for the FR shippers that take into consideration the FR shippers' current needs and use of the system on a seasonal basis. It is therefore consistent with the policy of protecting the captive customers' historical service. Moreover, in this case, the Commission is affording the FR customers additional protections and is giving these customers a preferential opportunity to obtain capacity from El Paso above their new CD entitlements. Therefore, the Commission is directing El Paso to make additional capacity available to the FR customers through capacity turnback, adjustments for seasonal usage, and a priority for capacity under the Line 2000 PowerUp. These steps will assure that all FR shippers will receive a fair allocation of available capacity needed to meet their load requirements.

The capacity rationalization process approved in this order will enable the FR shippers to receive service at the capacity levels they used on the system in 2001. Therefore, the Commission is approving a capacity allocation method that will continue service at existing levels, consistent with the abandonment protection.

3. Modification of the Settlements to the Extent Necessary to Convert the FR Contracts to CD Contracts is Just and Reasonable and in the Public Interest

The FR customers also argue that adoption of El Paso's proposal would unlawfully abrogate both the 1990 and 1996 Settlements. Southwest Gas argues that FR service is explicitly part of both Settlements, and any acceptable allocation proposal must preserve FR service rights, including the right to grow. APS/Pinnacle states that at the time of the 1996 Settlement, the FR customers agreed to pay millions of dollars to resolve the problem of capacity turnback in exchange for a guarantee of rate certainty and the firm

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[59]Order No. 637 at 31,339. This is consistent with the court's decision in Municipal Defense Group v. FERC, 170 F.3d 197 (D.C.Cir. 1999), upholding the Commission's decision in Texas Eastern Transmission Corp., 79 FERC ¶ 61,258 (1977), reh'g, 80 FERC ¶ 61,270 (1977), that small customers had special treatment for their existing service, but they must compete on an equal basis for additional capacity.

[60]Order No. 637 at 31,631-634.

capacity needed to meet their growing electric demands over the 10-year Settlement period. APS/Pinnacle states that the FR shippers would not have agreed to the 1996 Settlement if there had been a possibility that their rights as FR customers would diminish. The FR customers argue that modifying the Settlement halfway through its term is contrary to the public interest because it undermines the integrity of each settling party's firm contract and precludes the parties from recognizing the benefits of their bargains. They also argue that abrogating the Settlement would discourage settlements, contrary to the Commission's policy of favoring settlements.

It is the Commission's policy to encourage settlements[61] and the Commission is extremely reluctant to alter a settlement during its term. However, the circumstances on El Paso have changed drastically since the Settlements were executed. El Paso benefitted from the customers' sharing the risks and costs of the unsubscribed capacity. The customers benefitted from rate stability. FR customers were allowed to retain their FR contracts even though at the time of the Settlement, most other pipelines no longer offered FR contracts.[62] All customers realized benefits from the flexibility resulting from a largely unsubscribed pipeline. Finally, all customers benefitted from the revenue sharing provision,[63] since El Paso was able to sell its unsubscribed capacity at maximum tariff rates.

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[61]In this proceeding, the Commission encouraged the parties to resolve the capacity allocation issues on El Paso by settlement. After numerous attempts to settle these issues, including referral of the issues to the Commission's Dispute Resolution Service, the parties were not able to reach an agreement. At the same time, the situation on El Paso is, in the words of one of the FR customers, in a crisis, and action must be taken to resolve the issues.

[62]Instead, most pipelines offer fixed levels of no-notice service.

[63]The 1996 Settlement resolved the capacity turnback problem through an agreed-upon sharing of the risk of unsubscribed or undersubscribed capacity. Specifically, the 1996 Settlement provided that during the first eight years of the Settlement period, El Paso's customers would be responsible for 35 percent of the revenue loss assignable to unsubscribed capacity, while El Paso would bear 65 percent of that loss. As a quid pro quo, customers would share 35 percent of the revenues from future sale of the unsubscribed capacity exceeding a specified "Revenue Crediting" threshold. In addition, El Paso's historical firm customers agreed to pay an additional risk sharing amount of approximately $250 million. After the first eight years, El Paso would be at risk for 100 percent of the loss from unsubscribed capacity.

While the Settlement was a reasonable resolution of the issues facing El Paso and its customers at that time, the circumstances that made the Settlement reasonable do not exist today. Instead of facing capacity turnback, El Paso lacks sufficient capacity to meet the demands of its firm customers. As explained above, the result has been that there are regular cuts in firm service on El Paso, and firm service is not reliable. Unless the Commission makes some adjustment to the terms of the Settlement to reform the FR contracts and establish specific receipt point rights, the problems of unreliability on El Paso will continue and worsen.[64]

While the Commission rarely alters an approved settlement, it has not only the authority, but also the responsibility under section 5 of the NGA to make an adjustment to a settlement if the terms of the settlement have become unjust and unreasonable and the settlement operates in a way that is contrary to the public interest.[65] The Commission has a responsibility to exercise its authority in the circumstances here to provide a solution to the capacity allocation problems on the El Paso system. The Commission has attempted to minimize changes to the Settlement while taking action to alleviate reliability problems. The Commission does not propose to alter the Settlement rates. The FR shippers will continue to benefit from the Settlement because they will continue to pay their current demand charges based upon their billing determinant levels. To the extent that establishing specific service entitlements under the existing FR contracts is a modification of the Settlement, that modification is necessary and is in the public interest.

4. Methodology for Converting FR Contracts to CD Contracts

A number of different entitlement allocation methodologies have been proposed during the course of the proceedings, some of which incorporated conversion of FR contracts to CD contracts and some of which did not. El Paso in its initial proposal filed March 28, 2001 allocated capacity based on billing determinants. FR shippers offered alternatives to El Paso's proposal using non-coincident peak demand. At the March 13, 2002 Commission meeting, the Commission advisory staff apprised the Commission of the alternatives and presented another solution that would convert FR service to CD service with entitlements reflecting latest practices and the Commission's traditional system peak allocation approach. At the April 16, 2002 public conference, the parties presented further variations to consider.

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[64]As discussed above, the demand under the FR contracts is expected to increase. FR shippers have now projected that their needs in aggregate will total 3 Bcf over the next few years, more than a 300% increase.

[65]E.g., UDC v. FERC, 88 F.3d 1105, 1131 (D.C. Cir. 1996).

The Commission will not approve El Paso's proposal to allocate capacity to the FR shippers at their billing determinant level. While billing determinants determine the current cost allocation to the FR shippers pursuant to the 1996 Settlement, they do not reflect the current use of the system. Use of billing determinants would ignore all growth that has occurred since the 1996 Settlement, and would be unreasonable. A reasonable conversion methodology should reflect the current practices of these shippers.

The Commission also finds that the proposals of Salt River and Southwest Gas to convert FR shippers to annual CD levels based on historical non-coincident peaks are not reasonable. Non-coincident peaks represent a shipper's peak demand for the year, the one day when a shipper experiences its highest demand for the year. Shippers are likely to experience non-coincident peaks on different days and sometimes different seasons of the year. It is for that reason that pipelines do not design their systems based on non-coincident peaks. To do so would result in a drastically overbuilt pipeline, because the pipeline would not need to serve each shipper's non-coincident peak on the same day. Because shippers have different customer mixes, different locations with varying weather patterns, and different access to alternate fuels and supplies, one set of shippers' high demand on a given day will often be offset by another set's lower demand. Shippers would likely be unwilling to pay the high costs of construction necessary to build and reserve capacity sufficient to serve non-coincidental peak demands. In addition, because there is insufficient capacity to serve both the CD contracts and FR non-coincident peak demands, use of non-coincident peak would result in a reduction of the CD shippers' allocation below the current CD level. The Commission finds that it is not just and reasonable to allocate less capacity to these firm CD shippers than the capacity for which they have contracted and paid.

The Commission believes that a reasonable conversion methodology reflects the current practices of the FR shippers within the current capacity and does not allocate less capacity to any shipper than it is paying for. A reasonable conversion methodology thus does not reduce CD shippers' entitlements, and does not reduce FR shippers' entitlements below their 1996 Settlement billing determinants.[66]

In this proceeding, full requirements shippers have raised two major concerns with the use of a system peak demand for allocation purposes. First, shippers express the need to reflect seasonal variations in their entitlements. They argue that some shippers are summer peakers (e.g., electric generation) and others are winter peakers (e.g., space heating)and that using shippers' seasonal needs to "sculpt" their entitlement allocations

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[66]To the extent El Paso can adjust demand levels to accommodate seasonal variations in FR customers' demands, it must do so.

will result in more equitable and accurate contract entitlements. Seasonal entitlement allocations will allow shippers to obtain capacity for the seasons or months that they need it, thus freeing capacity the rest of the year for use by other shippers with different seasonal needs.

Second, the shippers stress their individual peak demands (i.e., their non-coincidental peak) did not occur on the December 12, 2001 system peak day, and that use of such a system peak day demand does not reflect their needs. The Arizona Corporation Commission argues that adoption of an entitlement allocation based on the system peak day would lead to blackouts, curtailments, increased pollution, and significantly increased energy costs in Arizona.[67] In addition, FR shippers argue that they will be subject to significantly increased costs when they attempt to purchase additional capacity, because it will be a seller's market for capacity.[68] Further, they allege, the lack of a price cap on short-term released capacity will deter long-term releases and will allow releasing shippers to command high prices for peak capacity that the FR shippers will need to serve core needs.[69] El Paso Electric Company suggests that the appropriate level of contract demand might be the midpoint between a shipper's 1996 Settlement billing determinants and its non-coincidental peak.[70]

The conversion methodology shall initially allocate among the FR shippers the system capacity that is currently not under contract to CD shippers. Additionally, as discussed below, El Paso has been authorized to add 230,000 Mcf/d with its Line 2000 project. El Paso has dedicated the Line 2000 capacity for system use. That capacity is therefore available to be allocated to FR shippers to use this Fall. The full existing capacity plus the Line 2000 capacity minus the full CD shippers' contract levels and a reasonable amount to serve the FT-2 shippers, is the amount available to be allocated to the FR shippers at no additional charge above their current demand charge responsibility. The initial entitlements under the new CD contracts are, however, only the starting point for providing capacity to the FR shippers.

A capacity rationalization process, including capacity turnback, adjustments for seasonal usage, and capacity release, will provide additional capacity to meet FR demand. For example, Burlington Resources and other shippers indicated at the April 16 conference

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[67] Tr. at 50.

[68] Tr. at 78.

[69] Id.

[70] Tr. at page 107.

and in their written comments that they would be willing to turn back 725,719 Mmcf for the summer months and 592,719 Mmcf for the winter months.[71] In addition, El Paso offered, at the April 16 conference, to work with its shippers to "sculpt" (incorporate seasonal variations into) the FR entitlement allocations.

Other parties at the April 16 conference asserted that the customers themselves were better suited to determining their own needs and should have a part in the entitlement allocation process. After consideration of the comments, proposals, and alternatives, the Commission concludes that it is appropriate to take an approach that incorporates many of the ideas and responds to many of the concerns raised by various parties. As noted above, we will not order a reduction of CD service. In addition, we will not specify individual CD entitlements for the FR shippers at this time. It is the Commission's desire that the parties who utilize the system involve themselves in the solution. The Commission will therefore direct El Paso and its customers to take the available capacity remaining that is not contracted for FT-1 CD service (or needed to serve FT-2 demand) and allocate that capacity among the FT-1 FR shippers as their new CDs. At the public conference, El Paso remarked that it would be able to deliver 5,400 Mmcf/d with the capacity to be provided by the PowerUp on a peak day.[72] In this way the FR shippers can decide among themselves how to divide up the capacity and whether to use seasonal and/or annual entitlement allocations. This represents their initial entitlements and does not require a redistribution of demand charge responsibility.

We direct El Paso and its customers to meet as soon as possible and as often as necessary to establish CD entitlements for each FT-1 FR shipper. The meetings should be in El Paso's service territory to facilitate participation of the parties' business and technical staff.

Once the initial CD entitlements are set, El Paso is directed to initiate a capacity rationalization process, as discussed at the April 16 conference,[73] in which current shippers are afforded an opportunity to turn back capacity, and converting FR shippers can purchase that capacity to augment capacity assigned during the conversion process. For the initial CD entitlements, the Commission will not require that costs be reallocated (although the parties may agree otherwise). In that way, the FR shippers are converted to CD entitlements at levels that can reliably be met at no additional charge above the Settlement rates. For any capacity purchased through turnback or capacity release, the

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[71] E.g., Tr. at 137.

[72] Tr. at 17.

[73] Tr. at 17-21.

converting FR shipper would pay the appropriate reservation charge. As a result, while demand charge responsibility may shift from one shipper to another, the total cost recovery will be unchanged. El Paso will remain revenue neutral as a consequence of the turnback. Finally, once the capacity rationalization process is complete, El Paso will then allocate primary receipt point rights among all CD and converting FR shippers following an iterative process, described later in this order. After reviewing the April 30, 2002 comments which detail amount of capacity that the shippers are willing to turnback,[74] and the restated FR needs, it appears that there should be sufficient capacity available to meet current needs as a result of this process.

The Commission will require El Paso to file a report with the Commission by September 3, 2002, detailing the steps that were taken (the new CD entitlements, the amount of turnback, etc.) and indicating the new CD levels for the CD and former FR shippers resulting from the capacity rationalization process and the receipt right allocations for each shipper resulting from the iterative process. By August 1, 2002, El Paso must report to the Commission whether the parties have been able to agree upon FR customers' entitlements under the new CD contracts. If the parties are unable to agree to entitlements, the Commission will establish appropriate CD entitlements for the converted contracts and will issue a further order to specify how entitlements should be allocated.

We are mindful of the conflicting timing concerns of the CD and FR shippers. The CD shippers demand immediate action to end pro rata service reductions.[75] They seek assurances that the financial losses they have suffered over the past three years will come to an end. The FR shippers, on the other hand, demand sufficient time to prepare for a limit to FR service.[76] They argue that they have made significant financial investments (for example, to build new generation plants) in reliance on the terms of the 1996 Settlement which ensures continuation of full requirements service through December 2005. They also argue that time is needed to arrange for alternate supplies and services if they are allocated less capacity than is needed to serve their core needs. The Commission finds that it is paramount to restore certainty and reliability to firm service on El Paso's system. We will therefore order FR service to be converted to CD service effective November 1, 2002. CD shippers will thus have certainty going into the winter heating

[74]The comments reflect that the shippers, in total, may be willing to turn back over 725,000 Dth/d of summer capacity and close to 600,000 Dth/d of winter capacity. See commends filed by Burlington, Dynegy, Aera, Coral Energy, Occidental, Texaco, ONEOK, Southern California Generation Coalition, and Aquila.

[75]Tr. at 142, 146.

[76]Tr. at 57, 74-75.

season, and FR shippers, many of whom are summer peakers, will not be impacted this summer season and will have nine months to prepare for the 2003 summer season. In addition, the November 1, 2002 effective date will provide the parties the time to participate in the solution.

C. El Paso's Service Obligations

1. The Need to Make Additional Capacity Available to the Firm Shippers

All of El Paso's customers, both FR and CD, have argued in these proceedings that the capacity problems on El Paso have been caused, at least in part, by El Paso's failure to meet its service obligations to its firm customers. In Docket Nos. RP01-484-000 and RP01-486-000, the complaining shippers ask the Commission to order El Paso to expand its system and use that expanded capacity to satisfy its existing contractual obligations. The shippers argue that El Paso is obligated under Article 16.3 of the Settlement[77] to maintain quality and quantity of service. In addition, in Docket No. RP01-484-000, Joint Complainants argue that the Commission has authority under sections 5 and 7 of the NGA to require El Paso to comply with its certificate, contract, and Settlement obligations by ordering additional expansions and requiring the expansion capacity to be used to satisfy El Paso's existing firm contractual obligations.

Similarly, in Docket No. RP01-486-000, TNMA Shippers argue that El Paso has a legal obligation to maintain system capacity sufficient to meet all of its contractual commitments to provide firm transportation. They argue that a pipeline may be deemed to have violated section 7(b) of the NGA when the physical capacity of the pipeline is below the capacity required by its certificated contracts,[78] and that a pipeline is obligated to

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[77]Article 16.3 of the Settlement provides:

> 16.3 Service Obligations. El Paso agrees and confirms that, during the effectiveness of this Stipulation and Agreement, it will maintain and operate facilities sufficient to satisfy and perform the service obligations with respect to both quality and quantity of service imposed upon it by, and subject to the conditions applicable to, the provisions of this Stipulation and Agreement and its firm TSAs in effect on December 31, 1995.

[78]TNMA Shippers cite Columbia Gas Transmission Corp., 80 FERC ¶ 61,220 (1997).

maintain its facilities in a manner that will allow it to serve up to certificated levels or seek abandonment of capacity that was certificated but is no longer available.[79]

As an immediate step, TNMA Shippers ask that El Paso be required to dedicate the north-south capacity of its Daggett to Ehrenberg Line in California and the capacity it will be adding through compression to its new Line 2000 to fulfill its existing firm contractual obligations. Joint Complainants assert that any proposed expansion should be accompanied by a capacity rationalization process that would permit existing firm shippers to turn unwanted capacity back to the pipeline.

In the comments filed by the parties in connection with the April 16, 2002 public conference, the parties again argue that the Commission should require El Paso to meet its service obligations.

In its answers to the complaints, El Paso argues that it has provided firm service to FR and CD customers consistent with its contractual obligations, the capacity allocation provisions of its tariff, and the service obligation set forth in the 1990 Global Settlement. El Paso asserts that the parties to the 1990 Settlement specifically contemplated that a pro rata allocation of capacity might be required, and agreed to the allocation procedures now used by El Paso. In addition, El Paso asserts, the Global Settlement provides the circumstances in which it would be required to expand its system, and the parties agreed that El Paso would expand its system only when economically justified. El Paso states that the construction of additional capacity to serve the FR shippers at a commodity rate of two cents per Dth is not economically justifiable. Further, El Paso argues, citing Panhandle Eastern Pipeline Co. v. FPC, 204 F.2d 675 (3rd Cir. 1953), that the Commission does not have authority to order a pipeline to expand its mainline capacity. Therefore, El Paso asks that the Complainants' requests that El Paso be required to expand its system be denied.

However, since the filing of its responses in the complaint proceedings, El Paso has made a commitment to expand its transmission capacity by implementing its Line 2000 PowerUp project. At the April 16, 2002 public conference, El Paso committed that it would add up to 320,000 Mcf/d of new capacity through additional compression on its Line 2000 project.[80] El Paso stated that this additional compression, in combination with the proposal to convert FR contracts to CD contracts based on a system peak, should

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[79]TNMA Shippers cite Maritimes and Northeast Pipeline, L.L.C., 80 FERC ¶ 61,136 at 61,476 (1997).

[80]Tr. at 13-14.

eliminate the need for any pro rata allocations except in circumstances related to maintenance or force majeure.[81] Thus, while the Commission has stated that the decision whether to undertake to build additional capacity is a business decision that is left to the pipeline in the first instance under the NGA,[82] in this case, El Paso has committed to expand its capacity.[83]

The Commission further finds that El Paso, with respect to its obligation to provide firm shippers with the firm service for which they have contracted, must reasonably insure the quality of firm service, and that its actions do not degrade the quality of such service. In this regard, and in accordance with the provisions of the 1996 Settlement and the Commission's regulations, the Commission advises El Paso that it may not enter into new firm service contracts unless it can demonstrate that it has available capacity to provide the service.[84] Further, the Commission will require, during the pendency of the Settlement, that El Paso must first offer firm capacity that becomes available to existing shippers.

2. Flexible Receipt and Delivery Points

In Order No. 637, the Commission instituted proceedings to, among other things, review pipeline tariffs to insure shippers could flexibly and efficiently use the services for which they have contracted, and to insure there were no impediments to the use of third

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[81]Tr. at 14.

[82]E.g., El Paso Natural Gas Co., 54 FERC ¶ 61,316 at 61,924 (1991). See also Panhandle Eastern PipeLine Co. v. FPC, 204 F.2d 675, 680 ("Congress intended to leave the question whether to employ additional capital in the enlargement of its pipeline facilities to the unfettered judgment of the stockholders and directors of each natural gas company involved.")

[83]The Commission is committed to expediting the handling of El Paso's application for the PowerUp Project to ensure that the additional capacity is brought on-line as soon as possible. The Commission expects that El Paso will do all it can to expedite this process by filing a complete application. El Paso indicated in its August 23, 2001 data response that it could have an application before the Commission by March 2002, and stated at the April 16, 2002 public conference that it was preparing to file an application.

[84]This does not include capacity on lateral expansions to serve new markets, such as the Samalayuca lateral, 98 FERC ¶ 61,096, reh'g denied, ¶ 61,110 (2002).

party services. Several parties to these proceedings have voiced and filed comments (including Southwest Gas) requesting that El Paso be required to permit backhaul/displacement transactions from interconnections at or near the California border.

El Paso's tariff does not specifically allow such transactions. The Commission has found in numerous orders on Order No. 637 compliance filings, that pipelines must permit shippers to nominate service that would result in a change of flow under a service agreement. However, pipelines are not required to accept or permit backhaul transactions to the extent such transactions would negatively impact forward haul transactions or could not be operationally guaranteed. Further, in these orders, the Commission has recognized that backhaul nominations under what would otherwise be a forward haul transaction, fundamentally change the transaction, and only need be provided on a secondary priority basis. While the Commission has not completed its review of El Paso's Order No. 637 compliance filing, it must revise its tariff to permit those nominations and transactions. To the extent customers can avail themselves of these transactions, they may be able to increase capacity utilization of the El Paso system and gain access to gas storage facilities in California.

3. Demand Charge Credits

Joint Complainants assert that it is unjust and unreasonable for El Paso to charge for firm service that it does not provide. They assert that by overselling its system, failing to limit FR usage to a reasonable level, and selling 1.2 Bcf of available capacity to its affiliate, El Paso is reaping a windfall at the expense of the CD shippers who cannot use the firm capacity for which they are paying. Joint Complainants argue, citing Tennessee Gas Pipeline Company,[85] that El Paso should be required to credit firm transportation demand charges for any firm service that it cannot schedule for any reason other than force majeure.

In response, El Paso argues that pro rata allocation of firm service was specifically contemplated by the parties to the Settlements, and that El Paso has complied with the terms of these Settlements, its contracts, and its tariffs in providing firm service to its CD customers. El Paso states that the Commission has addressed the issue of whether a pipeline is obligated to issue demand charge credits in the context of each pipeline's tariff and service agreements. El Paso argues that in this case the Joint Complainants have pointed to no provision of the tariff, the service agreements, or the settlements that sets forth an obligation of El Paso to waive demand charge payments in the event the shipper's nomination is not scheduled due to the pro rata procedures. El Paso states that since the

[85] 71 FERC ¶ 61,399 at 62,580 (1995).

CD customers were aware of the possibility that their receipt point nominations might not be scheduled because of the capacity allocation procedures in El Paso's tariff, it was incumbent on them to insist that the Global Settlement provide them with the demand charge credits that they now seek. El Paso argues that because it has complied with its contractual, tariff, and settlement obligations, no demand charge credits can be ordered in this proceeding.

El Paso further argues that in the Tennessee decision cited by Joint Complainants, the Commission did not mandate credits in all circumstances other than force majeure, but instead stated that a pipeline should be able to perform the service it has contracted to perform. El Paso states that in these circumstances it is performing the service it contracted to perform, in accordance with the allocation provision of the Settlement. El Paso states that the flaw in Joint Complainants' argument is that they assume that because gas does not always flow on the basis of their nominations, it follows that they have not received the service that they contracted to receive.

The nature of firm service is set forth in the Commission's regulations: firm service is service that is not subject to a prior claim by another customer.[86] As explained above, firm service has the same attributes and must meet the same requirements on all pipelines. There is not a different type of less-firm firm service on El Paso. A shipper contracting for firm service, as compared to interruptible, pays the pipeline a charge to reserve capacity on the pipeline in addition to the volumetric charge for actually transporting the gas. If the reservation portion of the firm transportation rate does not in fact reserve capacity on the pipeline, that charge is unjust and unreasonable because the shipper is paying for a service that it does not receive. If a shipper is not guaranteed capacity on the pipeline to transport its contract demand, then the service is not firm service, but is interruptible service. It is not just and reasonable to charge a shipper the higher firm rate if the service the shipper receives is interruptible.

In the Tennessee decision cited by the parties, the Commission stated that pipelines should be able to provide the service they have contracted to perform, and that it is therefore reasonable for pipelines to provide demand charge credits when they interrupt service that they have contracted to perform, except where service is interrupted by force majeure. Contrary to El Paso's argument, this decision was not based on the particular provisions of the contracts involved, but on the nature of any contract for firm service. If firm service is interrupted to schedule service for another customer, that service is not firm and is not the service for which the CD customer contracted and pays.

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[86] 18 C.F.R. § 284.7 (2001).

A pipeline should not contract to provide more firm service than it has the capacity to provide. If El Paso sells more firm service than it can provide, and if it collects reservation charges for capacity that cannot be reserved, it is charging the customers an unjust and unreasonable rate. El Paso reasonably applied the Settlement provisions concerning pro rata allocations where there was insufficient capacity to meet demand for firm service. However, the Settlement provisions regarding pro rata allocation have led to the unreliability of firm service on El Paso and are no longer just and reasonable. Therefore, El Paso must prospectively provide firm service as contemplated by the Commission's regulations. When it is unable to do so, El Paso will be required to provide charge credits to its CD customers when it is unable to transport nominated volumes for reasons other than force majeure.

After the allocation process is complete, shippers will have specific receipt point rights at individual pools. The aggregate rights at any given pool should not exceed the maximum capacity at that pool or the mainline capacity for El Paso to transport the aggregate volumes. Therefore, after the capacity rationalization process is complete, El Paso should be able to transport all nominated volumes, except in circumstances of force majeure. We will direct El Paso to credit firm transportation reservation charges for any firm service that it cannot schedule for any reason other than force majeure, after November 1, 2002. El Paso shall file revised tariff sheets to reflect this reservation charge crediting requirement.

In addition, KN Marketing asked the Commission to order El Paso to refund all reservation charges KN Marketing has paid with respect to allocations that were not excused by force majeure in the East End. As explained above, the Commission is acting under section 5 of the NGA to establish just and reasonable allocation procedures on El Paso, including the crediting of demand charge credits for firm service that is not scheduled for reasons other than force majeure. Refunds are not available under section 5, and therefore KN Marketing's request for refunds is denied. Revenue credits will be available on a prospective basis.

D. Pooling

In its Topock order, the Commission found that El Paso's current capacity allocation methodology is unjust and unreasonable because it creates uncertainty with respect to the rights of firm shippers to receive firm service. The Commission required El Paso to file a proposal to allocate specific receipt point rights to its customers. The March 28, 2001 proposal filed by El Paso in compliance with the Topock order sets forth a methodology for assigning specific receipt point rights that is the subject of this order, as described more fully in Appendix A. The Commission has previously found that unspecified rights have led to the difficulties experienced in El Paso's primary pools.[87] The Commission finds the continuation of the practice of using unspecified receipt point rights is unjust and unreasonable. Based on the finding that systemwide flexible receipt point rights, as they operate on El Paso's system, are unjust and unreasonable, the Commission will direct El Paso to assign specific primary receipt point rights, as described more fully below.

1. El Paso's Proposal

In the March 28 filing, El Paso also proposes to change the number of pools on its system. El Paso proposes to replace the existing San Juan pools (Bondad and Blanco) with four pools (Bondad Station, Bondad Mainline, Blanco, and Rio Vista). The existing Anadarko pool would be replaced with three pools and the three Permian basin pools would be replaced with thirteen pools.

Pooling and the aggregation of supplies in the supply basins have been a long standing practice on El Paso's system that predates Order No. 636. El Paso's pooling points are located downstream of individual receipt points, where various supply sources merge or where pipeline capacity may be constrained. El Paso's current pooling arrangements encompass a vast network of liquid trading contracts and transportation contracts that come together in its current six basin pools. El Paso tracks these transactions. In the past, El Paso expressed concerns that the large number of pooling transactions can cause delays in the scheduling process. Additionally, El Paso has expressed concerns about matching customer supply rankings as a result of looped transactions.[88] El Paso indicates it was able to accommodate all pooling transactions, including unlimited looped transactions, when it had four days to schedule. Now with the standardized North American Energy Standards Board (NAESB) rules that provide for four intra-day nominations during the scheduling process, it has become increasingly difficult to track the pooling transactions when combined with downstream constraints that require El Paso to reduce customers' nominations pro-rata. El Paso indicates that pro-rata reductions are necessary due to force majeure or because shippers have nominated more

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[87] The Commission has previously indicated that the lack of specific receipt point rights creates uncertainty and is the main cause of the pro rata allocations based on nominations in El Paso's pools. See El Paso Natural Gas Company, 89 FERC ¶ 61,160 at 61,453 (1999).

[88] A looped transaction is one in which ownership of the gas may change several times without physical movement of the gas.

gas from a specific receipt point in the pooling area than the receipt point has the capacity to handle.[89]

El Paso states that its proposal would reduce the number of transactions in a pool and narrow the areas of constraint. El Paso states that its proposal to move from six to twenty pools is an attempt to achieve a compromise between service reliability and liquidity, preserving some of each. El Paso purports that smaller pools will provide more certainty and allow El Paso to better accommodate shippers' rankings of supply. El Paso states that it set the boundaries for its proposed twenty basin pools to group together system segments having similar operational characteristics.

El Paso cites the Bondad pool in the San Juan Basin to illustrate how it set pool boundaries. El Paso explains that it divided the Bondad pool into two pools: One north of the Bondad compressor station (Bondad Station pool) and one south (Bondad mainline). El Paso would allocate specific receipt rights to customers at the Bondad Station pool equal to the takeaway capacity at the compressor station. Prior to the division, Bondad shippers both south and north of the compressor station were included in the pro-rata reductions in the pool although the southern customers should not have been affected by the actual physical constraint at the compressor station. El Paso does not provide any other examples of constraints on its system justifying the expansion of pools in the other basins.

2. Customers' Response

Many commenters object to El Paso's proposal because they have different ideas about the appropriate balance between supply certainty and market liquidity. Some commenters, primarily those whose business relies on trading within the pools, believe that moving from six to twenty pools will unnecessarily reduce liquidity and the ability to aggregate supplies. Other commenters, primarily those who have contracts at specific plant outlets or wellheads, argue that receipts should be allocated back to specific receipt points to maximize reliability. Others would like the option of allocating to specific receipt points or pools.

The parties who commented on the pooling proposal uniformly object to El Paso's proposal to expand the number of pools.[90] The commenters conclude that 20 pools are not

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[89] El Paso data response filed August 23, 2001, Response to Question No. 2.

[90] In addition to individual comments opposing the pooling proposal, a diverse (continued...)

necessary, not justified, and not supported by El Paso's customers. The commenters further allege that a move to 20 pools will cause significant market harm.[91]

Parties assert that tripling the number of pools is an enormous and unprecedented change that greatly impacts existing contracts and the future deliverability of the pools. Commenters cite as an example the last pooling expansion on El Paso's system when El Paso divided the Keystone pool into three smaller pools. As a result of the split, liquidity in the two smallest pools (Plains and Waha) greatly decreased and trading was so de minimis that no monthly index is published for those pools. The parties point out that many of the new pools have few suppliers. They argue that six of the proposed Permian Basin pools would contain four or fewer receipt points[92] and that seven of the new Permian pools would handle a quantity of less than 300,000 Dth/d. They further argue that the Anadarko Dimmitt Pool would effectively have only one supply source because the upstream pipeline cannot physically deliver to El Paso at that point. By reducing the supply choices available in each pool, they argue that El Paso would create a fragmented market that would diminish reliability and price transparency and would give the remaining suppliers more opportunities to exercise market power and command higher prices. The commenters conclude that smaller pools can thus result in decreased reliability and higher costs to consumers.

In data responses, El Paso provided data demonstrating the frequency of constraints at the proposed 20 pools from July 2000 through August 2001. El Paso provided a chart that contains the total number of scheduling cycles where confirmed nominations (FT and IT) exceeded capacity.[93] El Paso explains that "a substantial majority" of those instances were the result of shippers using system-wide receipt point flexibility. El Paso states that if there were specific primary receipt point rights established in the pools, the number of reductions would be "drastically" reduced.

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[90](...continued)
group of El Paso's customers (including CD and FR shippers) filed joint comments on the pooling issues. See Initial Comments on Pooling Issues, filed April 16, 2002, by Conoco, Dynegy, PG&E, Duke Energy, Richardson, Texaco, Williams, Salt River, MGI, Aquila, Coral Energy, and Southern California Generation Coalition.

[91]Initial Comments on Pooling Issues at 2-3.

[92]Initial Comments of Parties on Pooling Issues, at 9 and 10.

[93] El Paso data response filed August 23, 2001, Response to Question No. 4.

Commenters argue that the data supplied by El Paso is flawed and does not justify the proposed 20 pools.[94] They argue that the data include nominations for both FT and IT service and thus do not indicate how much of the pro rata allocations were for firm nominations. They point out that El Paso has inflated the number of pro rata allocations by counting all four cycles of the gas day rather than daily reductions. They state that Permian Basin supply gas was curtailed during the period the data were provided due to the rupture at the Pecos Line just west of the Permian Basin. Also, Permian supply was in unusually high demand at that time due to the unprecedented high price of gas at the California border.

Commenters state that El Paso claims that its pooling proposal is in response to its customers' requests for El Paso to honor their supply rankings. Commenters assert that El Paso's customers would rather stay with the existing six pools, even if El Paso is unable to accommodate their supply rankings, rather than move to 20 pools and have El Paso more able to follow their rankings.[95] Commenters conclude that the Commission should direct El Paso to allocate specific receipt point rights and eliminate systemwide receipt point rights before pursuing such a dramatic change to its pooling structure.

3. Discussion

The Commission has previously found that primary point access by shippers to specific receipt points was necessary to eliminate or greatly reduce routine pro-rata allocation of shipper nominations, thereby improving the reliability of firm service on El Paso's system. Specific rights to receipt points or supply area pooling points may equally accomplish this objective. The Commission agrees with both El Paso and the parties that pooling allows broader access to supply aggregation necessary to accommodate shippers' needs for both competitive prices and supply reliability.[96] The Commission agrees with the parties that pools with few receipt points and small volumes cannot effectively support competitive gas markets. The Commission believes that price transparency and competitive supply markets enhance customers' ability to aggregate and choose supply sources while creating seamless transactions. Fragmented pools can compromise that objective and render the pooling concept useless.

The Commission recognizes that tripling the number of pools on El Paso's system could significantly impact customers and their existing supply contracts. The Commission

[94] Tr. at 209.

[95] Initial Comments on Pooling Issues at 22.

[96] See Transcontinental Gas Pipeline Corp. 86 FERC ¶ 61,175 at 61,613 (1999).

believes El Paso's pools should encompass a wide enough choice of supply sources to accomplish the objectives of price transparency and liquidity without sacrificing reliability of supply. Once physical pools are established, the Commission has determined that a showing of operational need is necessary prior to allowing modification to pooling areas.[97] The Commission finds that there is sufficient evidence to support El Paso's proposal to increase the number of physical pools in the San Juan Basin from two to four.[98] The data show constraints in the current San Juan pools.[99] It appears that if specific receipt rights are not assigned at the four proposed San Juan pools, daily pro-rata allocations of nominations may be likely to continue.

The Commission finds that there is insufficient evidence of an operational need to expand the Permian and Anadarko pools from four to fourteen. In fact, even El Paso agrees with the parties that no pro-rata allocations were needed for the Permian pool this past winter.[100] The Commission believes that allocating specific primary receipt rights to shippers in the existing Permian and Anadarko pools will resolve the overnomination constraints without compromising liquidity and supply choices. Based on the assertions of El Paso as well as its customers that the capacity allocation process will minimize if not eliminate current supply cuts in the pools, the Commission will reject the proposed changes to the Permian and Anadarko pools at this time, without prejudice to El Paso filing changes to its pooling structure at a future time with the necessary operational support, if circumstances warrant. Consequently, the Commission will authorize El Paso to operate eight pools: Bondad Station, Bondad Mainline, Blanco, Rio Vista, Anadarko, Plains, Keystone, and Waha.

We also believe that El Paso should be able to accommodate the shippers who do not desire flexibility but instead would like certainty at specific receipt points. It does not

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[97]See Nor Am Gas Transmission Co., 85 FERC ¶ 61,039 at 61,118 (1998) reh'g denied, 86 FERC ¶ 61,162 (1999).

[98]El Paso explains that there is a capacity of 675 MMcf/d upstream of Bondad Station but only 575 MMcf/d downstream of the station. Tr. at 213.

[99]Carla Johnson, representing a number of parties regarding pooling issues (Conoco, Dynegy, PG&E, Duke Energy, Richardson, Texaco, Williams Energy Marketing and Trade, MGI, Salt River, Aquila Energy, Coral Energy, and Southern California Generation Coalition) acknowledged constraints at Bondad. Tr. at 216.

[100] Tr. at 216. El Paso maintains, however, that the south system was not operating at capacity last winter, so the system was not tested. El Paso argues that it needs to program to anticipate times when the system is working at capacity.

appear to be inconsistent with the pooling approach used by El Paso to allow shippers to choose specific receipt points as opposed to pools. In fact, El Paso asked shippers to express such an interest.[101] If shippers desire access to only one receipt point upstream of a pool, and are able to contract with a particular source, it appears that El Paso should be able to accommodate such nominations. Therefore, El Paso is directed to make provision in its tariff and service agreements for a shipper to specify a point rather than a pool as a primary receipt point.[102]

E. Summary of Commission Actions

As discussed above, the Commission finds that the current daily allocation of capacity due to the lack of specific receipt point rights is not just and reasonable, and the Commission must act under section 5 of the NGA to direct El Paso to establish specific rights. Further, the Commission finds that continued unlimited growth in demand under the FR contracts does not send proper price signals for expansion of capacity, is not just and reasonable and is not in the public interest, and therefore, directs that the FR contracts be converted to CD contracts with a CD entitlement to be determined by the parties. The Commission also finds that it is unjust and unreasonable for El Paso to collect demand charges for service it cannot provide.

Based on those findings, the Commission directs El Paso to convert the Rate Schedule FT-1 FR contracts to CD contracts with specified maximum daily quantities (MDQs) and to assign receipt point rights utilizing the modified eight pools. The Commission directs El Paso to convert the current FT-1 FR contracts to CD contracts at a CD level to be determined by the parties. If the parties are unable to reach an agreement by July 31, 2002, El Paso must report to the Commission, and the Commission will issue an order to specify how capacity should be allocated on the system.

The Commission will preserve the status quo for small FR customers that take service under the FT-2 rate schedule. These shippers pay a volumetric rate for their service, and their peak loads are currently less than 8,000 Mcf/day. Therefore, these small load customers with minimal receipt rights do not have a significant impact on system use,

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[101] August 23, 2001 data response to Question No. 1.

[102] In the allocation process ordered in another section of this order El Paso would only assign an individual receipt point to a shipper after any pro-rata election process assuming that the shippers election was at the closest pool. No additional priority is awarded the shipper because of its more narrow election. However, after the allocation process, the shipper's primary receipt point rights would be at the point only, not the pool.

and continuation of their FR service for the remaining term of the Settlement will not have a negative impact on the remedy adopted in this order. We will require El Paso to establish a service eligibility ceiling quantity for the FT-2 Rate Schedule not to exceed 10,000 Dth/d.[103] Small FR shippers eligible for the FT-2 Rate Schedule may convert to that service in lieu of CD service.

Second, immediately after the initial conversion**,** but prior to the allocation phase, El Paso is directed to accept requests for turn back of existing contract quantities (from either existing or newly converted contract demand customers) and requests for additional contract quantities from FR customers. El Paso is directed to accept the capacity turnbacks to the extent necessary to satisfy the FR customers' requests for additional service.[104] Any shipper acquiring turnback capacity would assume the corresponding demand charge responsibility. In addition, shippers will have the opportunity to make available for posting permanent or long term release of capacity for either year round use or on a seasonal basis. This may allow summer and winter peakers to match their initial allocation to their individual peak needs.

Third, El Paso will allocate receipt point capacity in the modified eight pools[105] to all existing shippers based on their converted and existing CDs using the iterative process proposed by El Paso in its March 28 proposal.[106] In each round, each CD and converted FR shipper will nominate volumes at one or more pools of its choice, and El Paso will assign capacity on a one-time, pro-rata basis to each shipper at its selected pool. A round will be completed once each shipper has received either its full CD or no capacity remains at the selected pool.[107] No firm shipper is excluded from this process, including those who now have specific receipt point rights. Their existing rights are to be included with all

[103] See Order No. 636-A at 30,546.

[104] The acceptance of these requests for service will be subject to the creditworthiness provisions.

[105] Individual shippers would be allowed to select individual receipt points if they desire. El Paso will allocate this election by assuming the selection is to the closest pool and include the selection in that pools' pro rata allocation.

[106] This is the same process approved by the Commission in the Topock order.

[107] All shippers, including shippers who have current primary rights, are to participate in the pro-rata allocation.

other rights and allocated pro rata.[108] El Paso will then notify each shipper of the CD amount it received in each pool in the round. A subsequent round will begin with parties nominating any remaining CD amounts to remaining available capacity at available pools. Again, El Paso will assign capacity on a pro-rata basis until each shipper receives its full CD or no capacity remains at the receipt point. After the allocation process, each shipper will have specific receipt rights at individual pools. The aggregate receipt rights at any pool will not exceed the capacity at that pool so that pro-rata cuts should no longer be necessary, absent force majeure.

After completion of the allocation process, El Paso must provide an opportunity for shippers to trade allocations of primary receipt point rights. This will allow shippers again to match supply contracts with receipt points where they are allocated capacity. Further, the Commission will require El Paso to modify its tariff to permit use of secondary receipt points as available. The Commission will further require El Paso to immediately allow the use of its California delivery points as receipt points in order to promote exchanges from off-system deliveries.

El Paso will report the results of the conversion and the capacity rationalization process in a report to the Commission by September 3, 2002. The report should include, by shipper, the initial conversion entitlements, the contract demands after the capacity rationalization process, and the receipt point allocations. The new CD entitlements and receipt point allocations will be effective November 1, 2002.

The capacity allocation will not change the cost allocation of the system, except to the extent a shipper turns back capacity which is acquired by another existing shipper.

In recognition of the Settlement provision that commits El Paso to provide the full requirements of the FR shippers through the term of the Settlement, we will require El Paso to give existing shippers priority for any new capacity that El Paso might propose to construct through the term of the Settlement. Additionally, through the term of the Settlement, we will require El Paso to accept turnback to meet growth in the needs of its existing shippers. At least once a year, El Paso must determine whether any existing shippers require additional CD allocations and to solicit turnback of capacity to meet those additional requests. Any shipper that acquires such turnback capacity would assume the demand charge responsibility for that capacity.

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[108]Other FR shippers and CD shippers have also elected specific rights given the choice.

We will require El Paso to amend its tariff, effective November 1, 2002, to provide for refunds of demand charges to its customers on any day that El Paso is unable to deliver nominated CD volumes from a primary receipt point to a primary delivery point.

The remainder of the Settlement will remain in place (e.g., the Risk Sharing Mechanism, the fuel tracker, etc.). El Paso will continue to be responsible for crediting revenue to customers for the sale of firm capacity to reimburse shippers for the amounts they paid El Paso in the early years of the Settlement under the Risk Sharing Mechanism.

F. Need for an Evidentiary Hearing

Several FR shippers have argued throughout these proceedings that the Commission cannot resolve the capacity allocation issues on El Paso without first holding an on-the-record evidentiary hearing to resolve issues of material fact that they allege are relevant to an evaluation of the issues in these proceedings. Further, several commenters assert that the Commission must hold an evidentiary hearing to provide the parties with an opportunity to obtain through formal discovery operational data to enable them to propose an alternative to El Paso's methodology. In the comments filed in connection with the April 16, 2002 public conference, several parties including the Arizona Corporation Commission, argued that the Commission should hold an evidentiary hearing prior to changing the capacity allocation methodology on El Paso.

APS/Pinnacle list 21 issues of fact that they assert cannot be resolved without a hearing. These include whether El Paso oversold its system, whether there is an implied limitation on the growth that can be added under the FR contracts, whether the amount of growth under those contracts was anticipated, what is the appropriate method of reallocating receipt point rights, whether the assumptions behind El Paso's studies are reasonable, and whether the current capacity issues will be alleviated by a market downturn or other external events prior to the expiration of the Settlement.

Similarly, Southwest Gas argues that the Commission must hold a hearing to determine the exact operational capacity of El Paso, whether any shipper has been curtailed since the issuance of the Commission's decision in Topock, and if so, what injury resulted from the curtailment. In addition, Southwest asserts that a hearing must be held to determine the intent of the parties with regard to FR service under the Settlement, whether the Settlements obligate El Paso to construct additional capacity to meet the needs of its shippers, and whether El Paso unfairly profited from the Settlement. Further, it argues, if an adjustment is made to FR service, there must be an evidentiary hearing to determine whether El Paso should be required to reimburse customers for risk sharing dollars. Southwest Gas also argues in Joint Complainants v. El Paso that the Commission cannot place limitations on the FR contracts without holding an on-the-record hearing under section 7(b) of the NGA to address the existing and future needs of the FR customers and the ability of these captive customers to obtain service in excess of the limitation imposed in their contracts.

On the other hand, Indicated Shippers argue in their post-technical conference reply comments that an evidentiary hearing is not necessary to enable the Commission to prescribe just and reasonable capacity allocation procedures on El Paso.

The Commission finds that an on-the-record trial-type hearing is not necessary to resolve the issues raised in these proceedings. As detailed above, the Commission has adopted just and reasonable procedures to permit the parties to establish reasonable entitlements under the new CD contracts and for allocating the existing capacity on El Paso. If the parties fail to agree on an allocation method, the Commission will establish appropriate entitlements based on current demands; it is not necessary for the Commission to conduct a hearing to determine the precise westward and eastward capacity on El Paso prior to determining a just and reasonable method of allocating existing capacity.

Many of the issues that the parties allege require an evidentiary hearing have been resolved by the Commission as a matter of law or policy. Thus, the Commission has explained that the conversion of FR contracts to CD contracts is consistent with the Commission's duty to protect captive customers from the monopoly power of the pipeline. In addition, the factual issues raised by the parties are either not in dispute or are not material to the Commission's ruling. There is no dispute that there has been significant growth in the takes of the FR customers, that the circumstances on El Paso have changed dramatically since the 1996 Settlement was approved, and that the current capacity allocation methodology on El Paso has resulted in routine pro rata cuts to firm service nominations.

It is not necessary or material to the adoption of a just and reasonable capacity allocation methodology on El Paso for the Commission to determine whether El Paso has oversold its system, whether any shippers have been curtailed since the Commission issued its decision in the Topock proceeding, or whether the economic downturn or other external events might resolve the issues without Commission action prior to the expiration of the Settlement. Neither is it necessary for the Commission to hold a hearing to address alleged inadequacies in the studies submitted by El Paso. The parties have not been hindered in developing alternatives to El Paso's proposal. As set forth on Appendix A, there are a number of proposals before the Commission and many parties presented additional alternatives at the April 16, 2002 public conference. The Commission has properly resolved the relevant issues raised by the parties as legal or policy issues, and a hearing is not required to resolve any disputed issues of material fact.

In TNMA Shippers v. El Paso, the TNMA Shippers filed a motion to require El Paso to respond to initial data requests. El Paso opposed the motion. Consistent with our determination that there are no material issues of fact in dispute that require a hearing, the discovery motion is denied.

The Commission orders:

(A) El Paso's full requirements contracts are converted to contract demand contracts, effective November 1, 2002.

(B) El Paso will file a report with the Commission by August 1, 2002 if the parties cannot agree to entitlement levels, or by September 3, 2002 to detail the results of the capacity rationalization process as directed in this order.

(C) El Paso is directed to modify its Rate Schedule FT-2 to apply only to shippers taking less than 10,000 Dth/d.

(D) El Paso is directed to amend its tariff, effective November 1, 2002, to provide for demand charge credits to its firm customers whenever it is unable to transport nominated volumes for reasons other than force majeure.

(E) El Paso is directed to amend its Order No. 637 compliance filing in this proceeding as directed in this order.

(F) El Paso's capacity allocation proposal is accepted as modified in this order.

(G) Joint Complainants' request for relief in Docket No.RP00–484-000 is granted in part and denied in part as discussed in this order.

(H) TNMA Shippers request for relief in Docket No. RP00-486-000 is granted and denied in part as discussed in this order .

(I) KN Marketing's request for relief in Docket RP00-139-000 is granted in part and denied in part as discussed in this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.

APPENDIX A

The Capacity Allocation Proposals Before the Commission

While the parties to these proceedings disagree as to the causes and best remedies for the capacity allocation problems on El Paso, all agree that firm customers are not receiving the firm service for which they contracted, and that some changes must be made on the El Paso system. In addition to El Paso, Southwest Gas Corp. (Southwest Gas), Southern California Gas Co. (SoCalGas), and Salt River Project Agricultural Improvement and Power District (Salt River) submitted comprehensive capacity allocation proposals for the El Paso system. Other parties have made suggested modifications to these proposals and counterproposals in their comments. The complaints also propose actions that El Paso should be required to take to resolve the capacity allocation issues. The proposals of the parties are summarized below.

I. El Paso's March 28, 2001 Capacity Allocation Proposal

El Paso's proposal for a new system-wide allocation plan would allocate primary receipt rights for all FT-1 shippers at one or more of 20 pools. Primary receipt rights would be allocated to CD customers equal to their individual CD volumes and to FT-1 FR[109] customers equal to the billing determinants established in the 1996 Settlement. El Paso asserts that the billing determinants are the best proxy for the quantity of capacity rights each FR shipper subscribed to in the 1996 Settlement proceeding. In addition, under El Paso's proposal, FR shippers would have system-wide receipt rights for those volumes above their billing determinants used to serve primary delivery points. These system-wide rights for FR shippers would be scheduled as alternate rights but would be treated in scheduling as having a priority over any other firm contracts using alternate points, and ahead of all interruptible and overrun shippers. In other words, El Paso states, FT-1 FR shippers would have a primary secondary right to schedule all volumes they require above their billing determinant level.

El Paso’s proposal would modify the existing scheduling provisions of its tariff and allocate available capacity in the following order: 1) FT-2 Shippers using primary receipt and primary delivery rights; 2) FT-1 FR and CD shippers using primary receipt and primary delivery rights; 3) FT-1 FR shippers using alternate receipt rights and primary

[109] Rate Schedule FT-2 shippers, i.e., small load customers that pay volumetric rates, would continue to have system-wide receipt rights. El Paso states that the FT-2 shippers' loads are small and assigning each of them very small quantities of primary receipt rights across a wide array of receipt locations would result in a hodgepodge of minimal receipt rights.

delivery rights; 4) FT-1 CD shippers using alternate receipt rights and primary delivery rights; 5) FT-1 FR and CD shippers using primary receipt and alternate delivery rights; 6) FT-1 FR and CD shippers using alternate receipt and alternate delivery rights; 7) IT-1 shippers using grandfathered agreements; 8) IT-1 shippers using first come first served agreements; and 9) authorized overruns.

El Paso states that under its proposal, the amount of available capacity on its system to be allocated among all of its shippers would be determined using the summer flow sheet filed in El Paso's Line 2000 application in Docket Nos. CP00-422-000.[110] El Paso states that summer flow sheets were chosen because they represent the amount of capacity available on a year-round basis due to the impact of ambient temperatures on available capacity. El Paso states that additional capacity made available by lower winter temperatures would be used to offset maintenance outages to the benefit of shippers using primary firm capacity rights or, if not needed for that purpose, would be available to be used on an alternate firm basis or sold on an interruptible basis.

El Paso states that, consistent with the methodology used in allocating capacity at Topock, Arizona,[111] shippers would be permitted to elect receipt right preferences for allocating contract rights. El Paso would use a scheduling model to perform the allocation calculations. Shippers with receipt rights in a single basin would be allocated primary receipt rights pro rata among the pooling areas within that basin in proportion to each pooling area's design receipt capacity. All other shippers would be asked to provide to El Paso elections that specify receipt pools where primary rights are desired, the quantity of rights desired at those locations, and the locations to which those receipt rights are to be delivered. El Paso states that when all the elections have been received, they would be processed using the scheduling model to determine where elections exceed available capacity. All elections that exceed the available capacity at a particular location would be allocated pro rata using the current tariff provisions. El Paso states that after processing is complete, each shipper would be notified what portion of its election was successfully allocated. The shipper would then make an election among the remaining pooling areas in amounts not to exceed its unallocated capacity receipt rights. Any receipt capacity allocated to a shipper in an earlier round could not be reduced by the elections of shippers in later rounds. El Paso states that this multi-step, iterative process of elections and allocations would be repeated until each shipper's defined volumetric entitlement (full billing determinants or CD) was assigned to primary receipt locations.

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[110] 95 FERC ¶ 61,176 (2001). El Paso states that the north mainline capacity is shown on flow sheet FERC 1042. The south mainline capacity is shown in the Line 2000 filing.

[111] El Paso Natural Gas Co., 93 FERC ¶ 61,060 (2000).

El Paso does not propose to establish contract path rights on its system. El Paso states that there are currently 106 delivery points covered by FR agreements, and, as a result, the distribution of El Paso's delivery obligation changes daily. El Paso states that it cannot establish contract path rights on its system as long as the volumetric rights of shippers are not clearly specified.

El Paso asserts that its proposal will provide shippers with a greater degree of certainty in the scheduling process. However, El Paso states that there may be occasions when the distribution of the FR shippers' loads or a lack of displacement transactions will require El Paso to allocate capacity pro rata consistent with its tariff.

As stated above, El Paso submitted additional information and studies on its proposal in conjunction with the technical conference. Specifically, El Paso prepared several studies in response to requests made at the July 18-19, 2001 technical conferences. Each study allocates system receipt and delivery point capacity using the capacity allocation proposal filed by El Paso on March 28, 2001, but using varying assumptions. To simulate the allocation process, El Paso asked each FT-1 shipper to provide its supply preferences by ranking the proposed 20 pooling areas by order of desirability. If a shipper did not indicate a preference, El Paso used a default ranking. In each of the studies, El Paso allocated receipt point capacity up to the full contract demand for each current CD customer. The methodology used to allocate capacity to FR shippers varied from study to study.

In Study 1, El Paso allocated capacity to FR shippers based on non-coincident peak day demands, i.e., each customer's individual peak demand, during the test period for the Docket No. RP95-363-000 rate case. Study 1B allocated capacity based on coincident peak day demands, i.e., the system peak day, during the test period for the Docket No. RP95-363-000 rate case. Study 2 allocated capacity based on billing determinants agreed to in the 1996 Settlement. Study 3 allocated capacity based on non-coincident peak during the most recent 12 calendar months (July 2000 to June 2001). Study 3B allocated capacity based on coincident peak (i.e., system peak) during the same 12 month period. Study 4A based allocations on projected demand through the end of the Settlement (2005) regardless of whether the peak demand for such customer occurs in the winter or summer. Study 4B based allocations on projected demand based on the greater of the aggregate projected demand for the FR shippers reflected in Study 4A. Because the projections received by El Paso showed an aggregate winter load that was greater than the aggregate summer load, Study 4A was based on the projected winter loads for the FR customers.

In response to requests made at the August technical conference, El Paso submitted four additional studies. Study 5A based allocations to FR shippers on Winter 2000-2001 non-coincident peak demands. Study 5B was based on Summer 2000-2001 non-coincident peak demands. Study 6A was based on the average of the last five winter seasons' non-coincident peak demands. Study 6B was based on the average of the last five summer seasons' non-coincident peak.

In addition, El Paso proposes to increase the number of pools from the current six pools to twenty pools, and shippers would elect as their primary receipt points one or more of these twenty identified pooling areas. El Paso states that it established the boundaries for its proposed pooling areas by analyzing supply areas on its system and determining which receipt points could be grouped together as having similar operational characteristics. El Paso states that it believes that it has arrived at the right number of pooling areas to maximize shippers' flexibility in sourcing gas while working with the pipeline's configuration and its operational realities to provide more certainty in transportation services.

El Paso states that it selected the use of pooling areas rather than individual receipt points for several reasons. First, El Paso states, use of all 141 individual receipt points on the system would result in shippers holding small and often impractical volumes of receipt rights. Second, El Paso states, it determined that using 20 pools instead of the current six, would enable El Paso to more closely follow the priorities set by the pooling entities. Finally, El Paso states, because the 20 pools are based on potential constraint points on the system, El Paso believes that using these pooling areas will reduce the number of shippers affected by individual physical constraints on the pipeline. El Paso states that to the extent that a constraint does occur within a pooling area, only those shippers with receipt point capacity in the pooling area where the constraint occurs would be affected.

Comments on El Paso's proposal were filed by a number of parties.[112] Generally, the FR customers, i.e., the EOC Shippers,[113] APS/Pinnacle, El Paso Electric, Salt River,

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[112]Comments were filed by Aquila Energy Marketing Corporation (Aquila), The Arizona Corporation Commission (Arizona Commission), Arizona Public Service and Pinnacle West Energy Corporation (APS/Pinnacle), the CPUC, Duke Energy Trading and Marketing (DETM), East of California (EOC) Shippers, Enron North America Corp. (Enron), Indicated Shippers, MGI Supply Ltd. (MGI), the Public Utilities Commission of Nebraska (Nebraska PUC), jointly by Sid Richardson Energy Services Co., Sid Richardson Pipeline, LTD., Sid Richardson Energy Marketing, LTD (collectively Richardson), PG&E, Salt River, Southern California Gas Co. (SoCalGas), Southwest Gas, and Williams Energy Marketing & Trading Co.

[113]EOC Shippers are Apache Nitrogen Products, Inc., Arizona Electric Power Cooperative, ASARCO, Inc., BHP Cooper, Inc., Arizona Gas Division of Citizens

(continued...)

Richardson and Southwest Gas, and the Arizona Commission oppose El Paso's proposal to allocate capacity based on billing determinants. The CD customers, on the other hand, generally support allocating capacity to FR shippers based on billing determinants but object to the priority given to FR shippers in scheduling volumes above the billing determinants level. The comments of the parties are discussed in more detail below.

II. Alternate Proposals

Several parties offered alternative proposals in their post-technical conference comments. In addition, on November 13, 2001, Salt River filed a comprehensive capacity allocation proposal referred to as the "Strawman Proposal." Comments on the Strawman proposal were filed on December 7, 2001.

Southwest Gas, El Paso's largest FR customer, proposes to convert FR customers to contract demand service and permit FR customers to establish contract demands above their respective billing determinant levels by receiving an allocated share of the Line 2000 capacity (230,000 Mcf/d) and an allocated share of the Line 2000 Power-Up capacity (320,000 Mcf/d). The allocation of the Line 2000 capacity among the FR customers would be based upon cost levels that these FR customers have borne and continue to bear under the 10-year Settlement. Southwest Gas further proposes to cover the costs of the project through a surcharge to be imposed on the FR customers to recover the cost of service associated with the Power-Up capacity, as well as a base transportation charge. Southwest Gas' proposal includes a one-time trading procedure of monthly and seasonal capacity rights among converting FR customers.

Under Southwest Gas' proposal, receipt capacity would be allocated to FR shippers based upon their non-coincident peak quantities using data from the most recent twelve-month period. Receipt capacity for the CD customers would still be based on their CDs. Capacity would then be allocated based on the ratio of a shipper's individual CD or noncoincident peak to the sum of all CD and noncoincident peak quantities. Both CD and FR shippers desiring to nominate above their allocated receipt capacity would have to nominate the excess in a second round of nominations.

El Paso Electric proposes that El Paso be required to hold a special open season for FR shippers prior to allocating receipt capacity. Under this special open season, the CD

[113](...continued)
Communication Company, El Paso Electric Company, El Paso Municipal Customer Group, Phelps Dodge Corporation, PNM Gas Services, a division of Public Service Company of New Mexico, and Southern Union Gas Company.

shippers would be able to turn back capacity they no longer wish to hold, or simply release any excess capacity for a finite period of time. Only FR shippers would be permitted to bid for this capacity. Agreement reached tentatively in the open season bidding would be contingent on a FR shipper's willingness to convert its FR contract to a CD contract. If a FR shipper can acquire sufficient capacity either through turnback or release, then these shippers have the option to convert to a CD contract. This opportunity to convert status would be completely optional. Other proposals suggest capacity allocation on the average of the last five years non-coincident peak or on the basis of the higher of coincident peak for the past twelve months or billing determinants.

On November 13, 2001, Salt River filed its proposal. Salt River states that under its proposal, CD customers would retain their current CDs, while FR shippers would convert to seasonal entitlements based upon their historic reliance on the system, but weighted toward present use.[114] Under the proposal, Line 2000 capacity would be required to be brought into service promptly by El Paso, and El Paso would be directed to solicit turned-back capacity to meet shortfalls in firm requirements. The proposal provides for reservation charge credits for firm volumes not shipped. In addition, the proposal would allow shippers to segment their capacity on the Northern and Southern mainlines. The proposal would reduce the number of pools to two. A number of comments were filed on Salt River's proposal.[115]

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[114]FR customers would be required to convert to seasonal CD service with entitlements based on historical non-coincident peak, weighted to reflect current usage. Salt River used historical data from El Paso's studies (Studies 5a, 5b, 6a and 6b) for the 5-year period 1995 to 2000 to calculate each FR shipper's average quantities. For CD customers, Salt River used the current CD (July 2001) in the calculations. In the allocation mechanism the 5-year average non-coincident peak and the 2000 non-coincident peak for FR shippers were averaged, for the summer and winter, respectively, thereby weighting the conversion quantity to the current period. The 5-year average was given the same weight in the calculation as the 2000 non-coincident peak, i.e., the most recent year was given the same weight as the average of the last five years combined.

[115]Comments Salt River's proposal were filed on December 5, 2001, by Arizona Commission, AEPCO,Citizens Communications, APS/Pinnacle, California Parties (California Parties are SoCalGas, San Diego Gas and Electric Co. and the CPUC), Conoco, DETM, Panda Gila, El Paso, El Paso Electric, El Paso Municipals Customer Group (EPMCG), Indicated Shippers, MGI, Oneok Energy Marketing and Trading Co., L.P. (Oneok), PG&E Energy Trading-Gas Corporation (PG&E ET-Gas), PG&E, Phelps Dodge Corporation (Phelps Dodge), Public Service Company of New Mexico (PNM), Public Utilities Commission of Nevada (PUCN), Richardson, Southern California Edison

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III. Joint Complainants v. El Paso

On July 13, 2001, in Docket No. RP01-484-000, Joint Complainants,[116] a group of El Paso CD customers and the CPUC, filed a complaint challenging El Paso's capacity allocation procedures. These parties argue that El Paso has sold more firm capacity on its system than it can reliably provide, resulting in a violation of the pipeline's public service obligations and of its obligations under the 1996 Settlement. Joint Complainants assert that this alleged overselling of firm capacity, combined with the unlimited growth of the demands by the FR customers, results in unjust, unreasonable and unduly discriminatory services on the El Paso system, in violation of sections 5 and 7 of the NGA, as well as the Commission's regulations, the 1996 Settlement, and relevant principles of contract law which limit full requirements to reasonable levels.

Joint Complainants ask the Commission to provide a three-part remedy to resolve these violations. First, they ask the Commission to convert the FR contracts to CD contracts at a reasonable CD level. Joint Complainants assert that if FR demand by EOC shippers is permitted to continue to grow without limits there will be further erosion of firm service provided to El Paso's CD customers. Joint Complainants assert that a reasonable CD level would be a level equivalent to each shipper's billing determinant, or, for a transition period, 110 percent of the billing determinant level. Alternatively, Joint Complainants state that each FR shipper should be given the opportunity to utilize a seasonal CD entitlement that, on an annual average basis, would equal its billing determinant.

Second, Joint Complainants ask the Commission to order El Paso to expand its system to the extent necessary to enable it to meet its existing firm transportation obligations. Third, Joint Complainants ask the Commission to require El Paso to pay demand charge credits for firm volumes it does not transport for reasons other than force majeure.

El Paso filed an answer to the complaint. In addition, Texas, New Mexico, and Arizona Shippers (TNMA Shippers) and APS/Pinnacle filed comments in opposition to the complaint. Comments supportive of the complaint were filed by Midwest United Energy,

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[115](...continued)
Company (SoCalEd), Southern Union Gas Company (Southern Union) and Southwest Gas.

[116]Joint Complainants are Aera, Amoco, BP, Burlington, Conoco, Coral Energy, ONEOK, PG&E, Panda Gila, CPUC, SoCalEdison, SoCalGas, and Texaco.

L.L.C., Enron and Richardson. Southwest Gas filed comments in response to Enron's comments.[117] The arguments of the parties are discussed below.

IV. Texas, New Mexico and Arizona Shippers v. El Paso

On July 17, 2001, in Docket No. RP01-486-000, the Texas, New Mexico and Arizona Shippers[118] (TNMA Shippers) filed a complaint alleging that El Paso violated the Natural Gas Act (NGA) and breached its contractual obligations to its customers by failing to maintain its facilities in a manner that will allow it to provide firm service up to certificated levels. The TNMA Shippers argue that El Paso has a legal obligation under Section 7 of the NGA and Paragraph 16.3 of the 1996 Settlement to maintain system capacity sufficient to meet all of its contractual commitments to provide firm transportation service. TNMA Shippers request that the Commission direct El Paso to show cause why it should not be required to augment the capacity available for transporting current customers' entitlements by dedicating the southbound capacity of its new Daggett-Ehrenberg line in California and the added capacity recently proposed for its Line 2000 for use by its existing firm transportation customers rather than for new customers.

El Paso filed an answer to the Complaint. In addition, ONEOK, Indicated Shippers, SoCalGas, Richardson, and SoCalEdison filed comments on the complaint,[119] and timely motions to intervene were filed by many of the parties participating in the capacity

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[117]In addition, timely motions to intervene were filed by Aquila, Arizona Corporation Commission; AEPCO; Citizens Communications; Asarco and BHP; Dynegy Marketing and Trade (Dynegy); El Paso Electric; EPMCG; MGI; PG&E National Energy Group Companies; Phelps Dodge and Apache.; Phillips Petroleum Co. and Phillips Gas Marketing Co. (Phillips); PPL Energy Plus (PPL); New Mexico PSC; Nevada PUC; Saguaro Power Company (Saguaro); Southern Union; and Williams. Motions to intervene out of time were filed by Calpine Corporation (Calpine); DETM; Nevada Attorney General's Bureau of Consumer Protection; and Southern California Generation Coalition and Individual Members.

[118]The Texas, New Mexico and Arizona Shippers are Apache, AEPCO, Citizens Communications, BHP, El Paso Electric, EPMCG, Phelps Dodge, New Mexico PSC, Salt River, and Southern Union. For the most part, these shippers are full requirement customers located in Arizona, New Mexico, and Texas.

[119]Indicated Shippers filed separate motions to intervene in this proceeding.

allocation proceeding.[120] The Nevada Attorney General's Bureau of Consumer Protection and the Southern California Generation Coalition filed untimely motions to intervene. The arguments of the parties are discussed below.

V. KN Marketing v. El Paso

On December 16, 1999, KN Marketing (now ONEOK Energy Marketing and Trading Co., L.P.) filed a complaint with the Commission alleging that El Paso's allocation of firm mainline capacity on the east end of its system, i.e. the San Juan Basin to Texas, is unjust and unreasonable because El Paso sells firm capacity in excess of the available capacity. KN Marketing asked the Commission to order El Paso to refund all demand dollars KN Marketing has paid with respect to allocations that were not excused by force majeure in the East End. El Paso filed an answer to the complaint asserting that it has not oversold its system and that it has allocated its capacity consistent with its tariff, its contracts and the applicable Settlements.

As stated above, in its order in Amoco Energy Trading Company v. El Paso Natural Gas Co.,[121] the Commission held the issues raised in the KN complaint in abeyance pending examination of system-wide capacity allocation issues in El Paso's Order No. 637 proceeding.

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[120] Aera, Amoco and BP, Aquila, Arizona Corporation Commission, APS/Pinnacle, ASARCO, Burlington, Calpine, Conoco, Coral Energy, DETM, Dynegy, El Paso Merchant Energy, L.P. (El Paso Merchant), Enron, Exxon Mobil Corporation (Exxon), MGI, Midwest United Energy L.L.C. (Midwest Energy), Nevada Attorney General's Bureau of Consumer Protection, Oneok, PG&E, PG&E National Energy Group Companies, Phillips, PPL, CPUC, Saguaro, Richardson, SoCalEdison, SoCalGas, Southern California Generation Coalition, Southwest Gas, Texaco and Williams.

Timely, unopposed motions to intervene are granted by operation of Rule 214 of the Commission's Rules of Practice and Procedure. 18 CFR 385.214 (2001).

[121] 93 FERC ¶ 61,060 (2000), order on clarification, 93 FERC ¶ 61,222 (2000), order on reh'g, 94 FERC ¶ 61,225 (2001).

APPENDIX B

Summary of Comments Submitted Regarding the April 16th, 2002 Public Conference

On April 16, 2002, a public conference was held to receive feedback from all parties regarding alternatives to El Paso's capacity allocation proposal. In addition to the presentations made at the conference and recorded in the transcript, comments and reply comments were filed. As discussed in detail below, most CD shippers are generally in favor of converting FR service to CD service but request prompt action. The FR shippers oppose conversion and object to the proposed entitlements under the new CD contracts. Most of the parties oppose El Paso's proposal to increase the number of pools from 6 to 20.

FR Conversion

El Paso generally supports converting FR service to CD service and believes that use of system peak (the higher of December 12, 2002 coincidental peak demand or the 1996 Settlement billing determinants) is supported by the changed circumstances on El Paso's system. El Paso states that the allocation among FR shippers could be resolved at the negotiating table if the Commission institutes a capacity allocation mechanism. El Paso also is willing to assign rights at individual receipt points, agrees that the 1996 settlement should be kept intact to the maximum extent possible, and supports maintaining the FT-2 rate schedule. El Paso offers to implement a capacity rationalization process (accepting turn back capacity to meet requests for increased capacity) and to "sculpt" or allow shippers to establish seasonal contract demands. Any remaining capacity requests could be met by the Power Up project which would add compression to its Line 2000 project and increase capacity by 320,000 Mcf/d. El Paso is willing to forego cost recovery for the above mentioned system expansion until the next rate case if it receives a presumption for rolled-in rate treatment and commitments from its shippers not to challenge the prudence of the project in the next rate case.

OEMT, PG&E, PUCN, and Panda suggest that the Commission promptly order the conversion of FR contracts to CD contracts to restore certainty of flow for nominated firm service. Indicated Shippers, SoCalGas, Dynegy, and SCGC recommend capacity allocation changes as a necessary first step to pathing the system. Indicated Shippers state that the Commission should exercise its Section 5 authority to impose a reasonable limit on the demands of the FR shippers to convert their FR contracts to a defined quantity. CPUC and SoCalEd argue that allowing some FR shippers to take more service than they pay for is discriminatory and would shift costs to other customers resulting in some customers receiving less than what they pay for and others receiving more than they pay for. PUCN argues that existing CD customers should not be placed at a disadvantage to new CD customers in the allocation of capacity rights. SoCalEd argues that FR shippers should be converted to CD service at their BD level, or El Paso needs to build additional facilities.

The FR shippers,[122] CPUC, Indicated Shippers, SoCalGas, SoCalEd, Southwest Gas and El Paso Electric believe there is insufficient capacity to meet core customer needs. All of these parties believe El Paso has violated the settlement by not providing new facilities to meet the needs of its customers. They assert that limiting full requirements service would result in a significant, adverse financial impact on the Southwestern economy as a whole. Southwest Gas states changes in capacity allocation constitute contract abrogation and would result in severe shortfall in service to its residential customers because it is not based on non-coincidental peak requirements. Arizona Corporation Commission argues a change in capacity allocation would be harmful to the citizens of Arizona. For example, reallocating pipeline capacity would reduce access to pipeline capacity, thereby depriving Arizona of the essential supplies of natural gas needed to generate electricity used to heat and cool homes and fuel industries during peak periods. In addition, any change in capacity allocation must acknowledge Arizona's growth in population and energy use. Arizona customers are captive geographically and contractually to El Paso who is the only pipeline that serves the middle and southern portion of the state.

The FR shippers assert it is the Commission's most basic responsibility to protect captive customers from the exercise of market power. They argue that, given the removal of the price cap on capacity release, the releasing shippers are in a position to extort very high prices from all of the shippers desperate to meet their service needs without having alternative options and that shippers will be forced to purchase peak demand service at spot market clearing prices. The FR shippers point out that any pipeline capacity that is released will be available to all shippers, whether former FR shippers or others, so the former FR customers will have to outbid the merchant plants for pipeline capacity.

SCGC, PG&E, El Paso Electric, and Southwest Gas state seasonal needs should be used as a basis to establish firm capacity rights of FR shippers. The FR shippers state that the selection of a single date as a basis for assigning pipeline capacity rights is by nature arbitrary and likely understates actual usage due to the cuts that El Paso has had on its system. EOC states that human needs and critical customers are being ignored because the use of coincident peak and scheduled volumes is discriminatory. EOC shippers argue that the BDs cannot reflect entitlement since they merely were numbers used to allocate cost in the last rate case.

OEMT and Panda believe capacity rights should be rationalized and that El Paso should solicit capacity turn-backs from CD shippers. The FR shippers propose that all firm shippers on the system, both CD and FR, should specify the firm contract demand level of

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[122] Salt River Project, PNM, Phelps Dodge, EPMCG, Arizona Corporation Commission, Citizens Communications, APS/Pinnacle, and Southern Union.

capacity to which they are willing to commit. This election shall be binding and made within 6 months of FERC approval of settlement methodology. Second, any existing CD customer may reduce its current firm service capacity commitment on the El Paso system within 60 days, without penalty or exit fees. Any FR shipper may elect to terminate its agreement within 60 days, without penalty or exit fee. Third, all contract commitments from FR shippers committing to a specific CD level shall be for a term not less than 10 years. Any current CD customer proposing an increase in its firm capacity rights shall commit to a contract term of not less than 10 years for all of their contracted capacity. Fourth, seasonality and voluntary capacity turnback should be pursued. Fifth, FR shippers believe adding pipeline capacity via additional compression would help alleviate capacity constraints.

CPUC contends that California shippers cannot turn back capacity without a formal hearing authorizing service abandonment. However, if turnback capacity is allowed at the California border, CPUC contends the California shippers should have the first option to that turnback capacity. Finally, CPUC argues that if turnback capacity becomes available, FR service should not include the ability to provide electric power generation service back into California, which is above and beyond their specific customer needs. Conversely, SCGC believes capacity turnbacks would help provide relief by making scarce capacity available for more efficient use.

OEMT suggests that if the capacity turnback process is inadequate to meet all needs, El Paso should be required to construct additional capacity. El Paso Electric calls for El Paso to dedicate its Line 2000 to FR shippers and to build more facilities to meet the growing firm shipper demands. Southwest Gas recommends that: (1) El Paso be required to construct the Power-up capacity and allowed to recover its cost of operating that capacity through an incremental rate; (2) Power-up capacity be allocated among FR customers based upon a percentage of BDs or December 12, 2001 coincidental peak throughput; and (3) primary contract holders be allowed to trade seasonal or monthly rights as part of a negotiating or iterative nomination process. Finally, Southwest Gas states that if the Commission eliminates FR service, it must permit those customers to schedule their new contract demand transportation to delivery zones (i.e., by defining their mainline contract quantities on a zonal basis, not on the basis of existing scheduling delivery points).

Indicated Shippers, SoCalEd, SoCalGas, PG&E, and SCGC state that demand charge credits should be mandated for shippers that do not receive the FT capacity for which they have paid. Demand charge credits would give El Paso an incentive to expand its system to meet contractual obligations and a disincentive to sell additional FT service when it cannot meet its current FT obligations.

EPMCG shippers, who take service under Rate Schedule FT-2, support maintaining the status quo for FT-2 shippers. Indicated Shippers believe there should be some limitations to FT-2 service to provide certainty because their recent usage is nearly double their BDs.

PG&E and FR shippers suggest that the California delivery points should also be available as receipt points at which exchanges or backhauls from storage facilities or other pipeline systems could be more readily accommodated. Southwest Gas and FR shippers asks that El Paso be required to offer firm backhaul transportation from California points under existing transportation agreements. Indicated Shippers state that FR shippers should not be permitted to release capacity above their BDs.

Timing

Indicated Shippers and SCGC claim substantial financial harm because of El Paso's cuts in CD firm nominations. For the three-year period from 1999 through 2001, Indicated Shippers claim these cuts, as set forth in affidavits attached to their comments, have resulted in nearly $103 million losses of five types: (1) stranded demand charges and surcharges; (2) sellers' lost revenues; (3) buyers' increased costs; (4) additional manpower costs; and (5) other unquantifiable miscellaneous injuries. OEMT suggests that the Commission should act promptly on the damages pertaining to El Paso's failure to meet its firm service obligations to OEMT. SoCalEd and PG&E suggest that the Commission redress El Paso's past certificate and contractual violations. EOC shippers state that Indicated Shippers' calculations of financial harm do not consider the materially-increased profits that the shippers may have been able to achieve as a direct result of the shortages caused by El Paso's actions.

FR shippers agree that El Paso should undertake the necessary steps for system expansion. FR shippers state that El Paso should determine a reasonable timetable and designate a date by which all firm capacity commitments will receive full service. EOC shippers strongly urge that there be an opportunity for discovery through settlement, or alternatively a hearing, protected by confidentiality through which serious settlement or hearing discussions could occur.

FR shippers assert significant lead time for any remedy is needed to avoid operational chaos and to allow for finding some other way to get the same needed supply. CD shippers are concerned that the process may lag because FR shippers have an incentive to delay the capacity allocation process. EOC shippers suggest that before a settlement can be achieved, the Commission needs to establish the actual operational capacity on El Paso system and must determine whether El Paso has failed to meet its service obligations under the Natural Gas Act. El Paso replies that EOC shippers's are essentially announcing that they have no intention to be part of any cooperative resolution to the capacity allocation issues. SoCalEd suggests that a new rate case to address all of the issues is necessary. SoCalGas suggests that an audit team consisting of members of the Commission Staff and representatives of CD and FT-1 FR shippers be directed to audit nominations by FT-1 FR shippers from January 1, 2000, to the present.

El Paso Electric states that if the Commission cannot adopt other FR shipper proposed remedies, the existing settlement should be dissolved and a new rate case filing should be ordered. As part of a new rate case, El Paso Electric suggests an open season where FR shippers determine their needed CD capacity on a seasonal basis and capacity turnback would take place. In the alternative, El Paso Electric recommends awarding FR customers a quantity up to the midpoint between their BD quantity and their NCP quantity on a seasonal basis. PNM, El Paso Electric, and Southwest Gas suggest the Commission issue an order clarifying the outstanding legal and factual issues and setting the matter for hearing.

Pooling

Companies[123] argue that the Commission should reject El Paso's proposal to move to twenty pools. Companies contend El Paso's pooling proposal to increase the number of pooling points from 6 to 20: (1) reduces and restricts liquidity; (2) limits shipper flexibility to purchase gas, with no increased benefits; (3) would not reduce the number of transportation cuts on the El Paso system; (4) is counter to the goal of certainty of flow for firm service on El Paso; (5) reduces the number of buyers and sellers in each pool; and (6) creates fewer and incomplete pricing mechanisms. Companies also argue that allocating system capacity alleviates El Paso's stated need to create 20 pools. Further, OEMT contends that El Paso's proposal relies on receipt point capacity where little or no physical ability to receive gas exists. OEMT suggests that the Commission should establish contract paths on the system to facilitate capacity release as envisioned by Order Nos. 636 and 637.

Companies suggest that El Paso be required to allocate receipt rights among only the current six pools, which would resolve the bulk of the allocation problems on El Paso's

[123]The following companies include producers, local distribution companies, gatherers, end users, generators, and marketers, and also include both CD and FR customers: PG&E; DETM; Aquila; Coral Energy; Dynegy Marketing and Trade; Conoco; Texaco; Salt River Project; Energy Advocates LLP; MGI; Williams Energy Marketing & Trading Company; Southern California Generation Coalition; Richardson; SoCalGas; Indicated Shippers; Southern California Generation Coalition; Southwest Gas; and ONEOK.

system without negatively impacting gas competition. Panda Gila states that the proposal to increase the number of production area pools from 6 to 20 should be deferred, pending the outcome of other changes on the El Paso system (i.e., elimination of the FR contract status and assignment of specific pool rights).

APPENDIX C

Summary of Affidavits Submitted by Contract Demand Customers

In Docket No. RP01-484-000, Joint Complainants filed copies of affidavits of Penny Barry of BP Energy Company (formerly Amoco Energy Trading Co.), Robert Eason of Burlington Resources Oil & Gas Company, Nicholas Rassinier of Conoco, Inc., and Donald Lindquist of Texaco Natural Gas Inc. that had been previously filed in the proceeding in Amoco Energy Trading v. El Paso Natural Gas, Docket No. RP99-507-000, to show financial harm. Joint Complainants filed a second set of more recent affidavits on behalf of BP Energy, Burlington, Conoco, ONEOK, and Texaco to show that this harm has continued since the filing of the earlier affidavits. The affidavits set forth the level of cuts that these CD shippers have experienced on El Paso.

In its comments submitted at the public conference on April 16, 2002, Indicated Shippers provided additional updated information in affidavits attesting to the financial harm suffered by BP Energy, Burlington, Coral Energy and Aera, Occidental Energy Marketing Inc. (OEMI), and Texaco for the period from January 1, 1999 to December 31, 2001. The affidavits allege five types of financial harm, i.e., stranded demand charges, lost marketing revenues, increased costs associated with finding replacement supplies, additional manpower costs, and other miscellaneous costs, such as loss of contracts and missed marketing opportunities.

Finally, in response to a May 8, 2002 data request, additional documentation was filed by Indicated Shippers and SoCalGas.

The affidavit and additional documentation are summarized below by company.

BP Energy

The initial affidavit submitted for BP Energy (formerly Amoco Energy Trading Co.) in Docket No. RP99-507-000 states that at the time of the filing of the complaint in that proceeding, Amoco and Burlington had experienced cuts in Cycle 1 nominations as high as 57 percent at Topock. For the month of August 2000, Amoco's cuts for that delivery point averaged 48 percent, and cuts for gas nominated from San Juan to the east end averaged 33 percent. The affidavit states that financial harm to Amoco grew from $1 to $2 million annually to more than $6 million since KN's complaint filed against El Paso on December 16, 1999.

The second affidavit submitted on behalf of BP Energy states that it continues to experience significant cuts in its seven transportation contracts with El Paso for firm transportation service from San Juan, Permian and Anadarko basins to SoCalGas/Topock, Mojave/Topock, PG&E/Topock and SoCalGas/Ehrenberg. Cuts for the period January 1, 2001 through June 30, 2001 averaged approximately 16% or 18,000 Dth/d, which in turn resulted in stranded demand dollars of $299,000 for BP Energy and another $414,000 for the contracts under which BP Energy ships or manages as agent. In addition to these stranded demand costs, BP Energy states that it suffers financial harm consisting of lost revenues from being forced to find other less attractive markets for its production, or having to curtail production due to lack of alternative markets.

The affidavit submitted at the public conference on behalf of BP asserts that for the period January 1, 1999 through December 31, 2001, Cycle 4 cuts were 40,063,202 MMBtu. This is gas that BP nominated on El Paso, for which demand charges were paid, and El Paso was unable to deliver at primary delivery points. The affidavit further states that the total stranded demand charges related to CD volumes that were not scheduled were $10,132,998. Total lost revenues for BP associated with having to find other markets for gas (i.e., the difference between actual sales price to those other markets and the first of the month cost of gas plus any additional transport costs for moving to alternate markets) were $28,989,212. There were additional manpower costs and miscellaneous costs and harm associated with these cuts, such as missed opportunities.

Burlington

In the initial affidavit Burlington states that for the summer months of 2000, cuts under Contract No. 97YG (into SoCalGas/Topock) peaked at 66% in June, 58% in July and 58% in August. Cuts under Contract 97YW (SoCalGas/Ehrenberg) peaked at 45% in June, 47% in July and 47% in August. Cuts under Contract No. 97J4 (into Waha and other points on the east end of El Paso's system) peaked at 45% in June, 41% in July and 51% in August. Burlington states these cuts have caused significant financial harm, but offers no cost data in support.

The second affidavit submitted on behalf of Burlington states that for the three-month period since the reallocation of delivery rights at the SoCalGas/Topock delivery point effective April 1, 2001, nomination cuts for Burlington of gas sourced from San Juan under Contract No. 9M7Z averaged 26%, and nomination cuts of gas sourced from Waha averaged 5%. Nomination cuts of gas sourced from San Juan under Contract No. 97YW averaged 35%, nomination cuts of gas sourced from Waha averaged 5%, and nomination cuts of gas sourced from San Juan under Contract No. 97J4 averaged 10%. The affidavit further states that Burlington Resources' overall San Juan basin cuts over this period averaged 21%.

The affidavit submitted at the public conference on behalf of Burlington states that for the period January 1, 1999 through December 31, 2001 Burlington incurred cycle 1 cuts in excess of 150 Bcf, cycle 4 cuts in excess of 145 Bcf, and total stranded demand charges of $17,964,434.

Conoco

In the initial affidavit Conoco states that for the time period from May 1, 2000, through August 18, 2000, the cycle 4 scheduling cuts for Conoco's firm transportation contract with El Paso (9DWE back-haul firm Havasu transport) were 14% for May, 26% for June, 27% for July and 37% for the first 18 days in August. Similar to Burlington, Conoco states these cuts have caused significant financial harm, but offers no supporting cost data.

The second affidavit submitted on behalf of Conoco states that for the time period March 1, 2001 through June 30, 2001, the cycle 4 scheduling cuts under Conoco's Contract No. 9DWE were 37% for March, 40% for April, 10% for May and 15% for June.

Texaco

In its initial affidavit Texaco states that it has been cut since July 2000 an average of 50,000 to 60,000 MMBtu/d on Cycle 1 nominations for its 179,000 MMBtu/d of firm transportation on El Paso's system, with a delivery point at Topock, allowing for deliveries into Mojave, PG&E, and Southwest Gas. This represents a 34% cut of its firm transportation. Cycle 2 nominations have been cut by an average of 20,000 MMBtu/d. It was cut 12,500 MMBtu/d in July 2000 and 18,800 MMBtu/d in August 2000, resulting in financial harm of $350,000 in transportation demand costs. In addition, it has had to utilize 4 nomination cycles in order to flow as much transportation as possible, and purchase Permian gas at a premium price on cycles 2 and 3, resulting in additional costs of millions of dollars to Texaco and its affiliates. Two of Texaco's long-time fuel suppliers have notified it that they will no longer sell natural gas to Texaco because it is an unreliable buyer, unable to flow gas on a consistent basis.

The second affidavit submitted on behalf of Texaco states that between January 1, 2001, and July 9, 2001, Texaco incurred $1 million in stranded transportation demand costs, which does not include the cost to buy more expensive gas at the California border to cover the gas that did not flow. The average daily stranded firm transportation was as follows: 2,248 MMBtu/d in January; 5,002 MMBtu/d in February; 13,534 MMBtu/d in March; 18,239 MMBtu/d in April; 35,580 MMBtu/d in May; 20,384 MMBtu/d in June; and 18,096 MMBtu/d from July 1-9.

The affidavit submitted at the public conference on behalf of Texaco asserts that over the past three years, stranded transportation demand fees have resulted in $4.2 million in stranded costs, and that Texaco experienced an estimated $34 million (inclusive of stranded demand costs) needed to replace gas that did not flow under the firm transportation agreement with Texaco.

ONEOK

The affidavit submitted on behalf of ONEOK states that scheduling cuts for seven contracts of ONEOK for the period March 2001 through June 2001 were as follows: for Contract No. 9DQH, 5% in March, 13% in April, 11% in May and 21% in June; for Contract No. 9KQX, 8% in March and April, 15% in May and 3% in June; for Contract No. 9M8X, 22% in April, 20% in May and 49% in June; for Contract No. 9M88, 23% in April, 10% in May and 2% in June; for Contract No. 9M89, 19% in April, 18% in May and 2% in June; for Contract No. 9MG6, 9% in April, 11% in May and 2% in June; for Contract No. 9M84, 10% in April, 9% in May and 35% in June.

Coral and Aera

Similarly, the affidavit submitted at the public conference on behalf of Coral and Aera states that Cycle 4 cuts for this period where Coral or Aera was the shipper were 6,013,222 Dt, and the total stranded demand charges were $659,992. Lost revenues associated with having to find alternative markets were $797,204.95, and lost revenues associated with having to find alternate suppliers were $2,966,463. The affidavit also states that there were additional costs associated with manpower.

OEMI

The affidavit submitted on behalf of OEMI states that for the period of January 1, 1999 through December 31, 2001, OEMI experienced total volume cuts of 1,212,394 MMBtu and total stranded demand charges of $432,590. Lost revenues associated with having to find alternative markets were $1,079,338. The affidavit further states that OEMI incurred additional manpower costs.

SoCalGas

In its May 15, 2002 data response, SoCalGas provided calculations supporting its claim of stranded demand charges. SoCalGas calculates that total stranded demand charges resulting from Cycle 4 cuts (taking the difference between what was nominated in Cycle 1 and what was scheduled in Cycle 4) were $27.8 million for the years 1999 through 2001. SoCalGas estimates its replacement costs of gas to be $164 million for those years.

Indicated Shippers

In its May 15, 2002 data response, Indicated Shippers filed additional data in the form of invoices and further explanation to substantiate the earlier affidavits filed by BP Energy, OEMI, and Texaco. BP Energy points out that one of its transportation contracts (97JB) has the San Juan Basin as its only primary receipt point yet it consistently receives monthly curtailments. Texaco elaborates that it was damaged in 32 out of 36 months and stranded almost 12 Bcf of gas transportation.